University of Alberta

The Influence of Organizational Forms and Client Relationships on Professional Behaviour: The Case of Enron

by

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Abstract

This thesis examines the factors that influence professional behavior. Specifically, it focuses on the role of organizational forms where professionals work and client relationships. Transcripts of Congressional Hearings related to Enron form the empirical context. Theoretically the thesis draws upon the research on the sociology of professions by revisiting the literature on professionals and organizations and professional-client relationship to suggest that the notion of professional behavior is more complicated than previously assumed.

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Chapter 1

Introduction

My interest in professional behavior was stimulated when the Enron debacle happened. Enron Corporation was an American energy company based in Houston, Texas, United States. Before its bankruptcy in late 2001, Enron was one of the world's leading electricity, natural gas, pulp and paper, and communications companies, with claimed revenues of $101 billion in 2000. *Fortune* named Enron 'America's Most Innovative Company' for six consecutive years. It achieved infamy at the end of 2001, when it was revealed that Enron's reported financial condition was sustained mostly by institutionalized, systematic, and creatively planned accounting fraud.

Investigations into the affair revealed that a group of Enron executives: in-house accountants and attorneys; along with management personnel with professional backgrounds, had been worried about the accounting practices from as early on as 1998. Despite communicating their apprehensions to top management, the auditors and even the associated law firm, their concerns were explicitly ignored for a long time. With increasing numbers of such Enron personnel continuing to disapprove, in August 2001 the CEO instituted an internal investigation headed by Vinson & Elkins LLP, one of the most prestigious law firms in the United States. The two-member team had access to internal accounting as well as to the auditors' documents. Yet, after a month, the Vinson & Elkins lawyers gave Enron's accounting practices and Arthur Andersen a clean chit. It later came to light that the scope of the investigation was substantively restricted through mutual agreement between the law firm, members of the top management and Arthur Andersen, Enron's auditor.

Arthur Andersen further surprised people by destroying Enron related documents just when the SEC was investigating Enron. In 2002, Andersen, one of the Big Four accounting firms, was convicted of obstruction of justice. The firm agreed to surrender its licenses and its right to practice before the SEC on August 31st, 2002. Arthur Andersen lost nearly all of its clients when it was indicted, and there are over 100 civil suits pending against the firm related to its audits of Enron and other companies. Fallout from the scandal quickly extended beyond

Enron to all those formerly associated with it. Large prestigious investment banks such as Barclays, Deutsche Bank, JP Morgan, Citigroup, Merrill Lynch, Lehman Brothers, Bank of America, and Canadian Imperial Bank of Commerce were held responsible and fined heavily. Prestigious law firms such as Vinson & Elkins and Kirkland & Ellis faced multiple lawsuits for being accessories in corporate fraud. Premier credit rating agencies such as Standard and Poor and Moody's and reputable financial analysts were criticized for being lapse in providing objective information about the organization. The enormity of loss and suddenness of the Enron debacle, took most people by surprise. Despite having one of the biggest accounting firms as an external auditor, having elite and well connected law firms as external counsel, and associating with some of the best known banks (i.e., JP Morgan and Citigroup), Enron collapsed. It left behind $15 billion in debt, worthless shares, and 20,000 workers who lost their jobs.

What I found most perplexing in this entire affair was the range and extent of professional involvement. I could not understand why elite professional service firms would endanger their reputation, arguably their core asset, to acquiesce and participate in potentially damaging activities. Enron's collapse was argued by some to be simply a business failure due to a series of bad management decisions, but in time it resembled a systematic collapse of a group of key gatekeepers (Coffee, 2003) who should have been able to recognize the signs. As part of an effort to unravel and make sense of the event, Congress launched a series of hearings right after Enron filed for bankruptcy. These hearings lasted for over a year. They focused on investigating responsibility of the auditors, destruction of Enron related documents by Arthur Andersen, and the terms of association between Enron, the financial institutions and analysts. These hearings are repositories of information because they provide access to a wide variety of data from official documents to memos, policies and personal communications. Most of the key players involved in this event also offered accounts and justifications of the actions they took.

As I followed these hearings, I found two interesting features. First, professionals from elite professional service firms (PSFs) defended their actions by highlighting their adherence to widely accepted rules of their parent profession. I was surprised by the lack of any acknowledgment of public responsibility in their accounts. This version of professional

behavior was not restricted to a particular profession but was common across professionals in elite professional service firms. Not surprisingly, these accounts failed to elicit much support and fell short of convincing both the Congressional members and the public. The subsequent indictment of Arthur Andersen was in some ways, an expression of the disbelief regarding its assertion of professional behavior. Furthermore, even while there were indications that some professionals were troubled by developments in Enron (especially in Arthur Andersen and in Vinson and Elkins) the organizations did not heed their concerns. For professional organizations built on valuing professional norms of autonomy, discretion and self-regulation, the failure to address concerns about accounting and financial structures highlighted a discrepancy in professed and dominant norms.

Moreover, as much of the defense of the professional organizations revolved around highlighting their reputation and status I wanted to understand the dynamic between these organizations and their equally reputable client. More specifically, I wanted to understand how the manner in which the interests between professionals and clients are negotiated results in marginalizing notions of objective professional judgment and investor trust.

To explore the question of professional behavior, my study examines the organizational forms that professionals work in, and professional-client relationships, both of which impact professional work. A focus on professionals in organizations highlights the importance of understanding the immediate context of professional work. Different organizational forms have unique features that influence professional behavior in different ways. A complementary approach to exploring professional behavior is to focus on professional-client relationships to see how variables beyond the employing organization impact upon their behavior. In other words, I propose to explore two sets of phenomena that affect professional behavior: the organizational context and relationships with clients.

The idea that professional behavior is influenced by a combination of factors is not exactly novel. In 2004, Greenwood and McDougald proposed focusing on the professional field (consisting of educational institutions, employing organizations, clients and the professional association) in order to understand the joint and possibly competing influence on the "technical and normative socialization of professionals" (2004; pg 2). My thesis focuses on

the Enron failure and examines the influence of the employing organization and clients on professional behavior. It explores the aspects of employing organizations and client relationships that influence professionals' conception of professional responsibility (Figure 1A). In the remainder of this introduction I briefly summarize weaknesses in the existing literature on this topic.

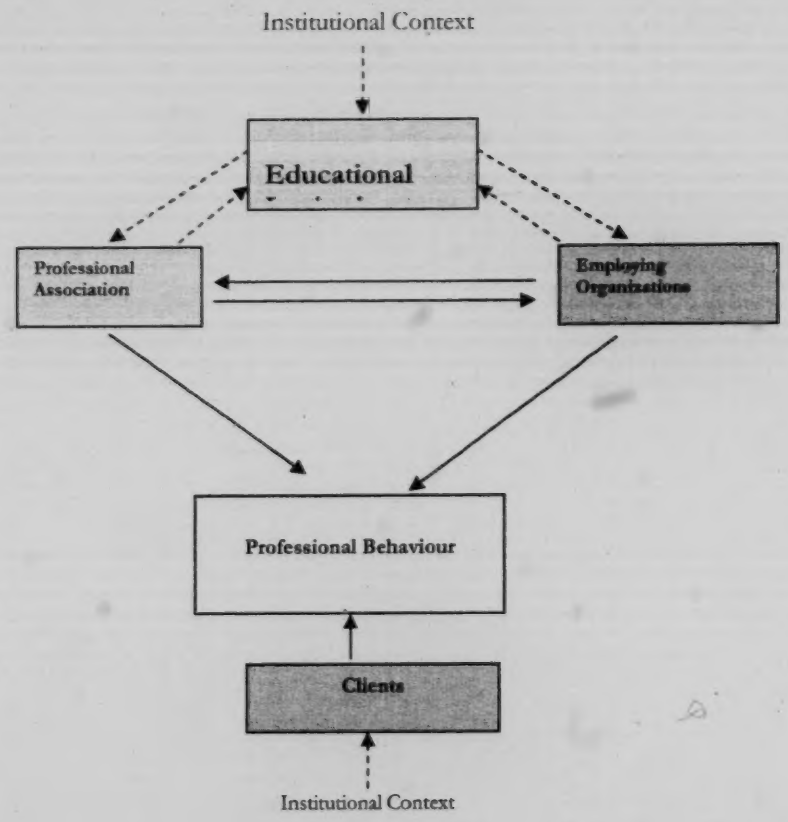

Figure 1A
Variables Influencing Professional Behavior (Adapted from Greenwood & McDougald, 2004)

Overview of Issues

Professional Behavior

Professional behavior has had an interesting history within the sociology of professions literature (Meadows, 1946; Milton, 2006; Ottaviani & Sorensen, 2006). In 1915, Abram Flexner proposed seven criteria of professionalism which included: technical competence; educationally transmissible content and technique; a body of scientific data with critical analysis; and a public welfare motivation. The social service motive, "assumed to be universal in professions and virtually non existent in business, usually receives top billing" (Meadows, 1946). In his work, Meadows suggests that professionalism is a concept, 'that expresses a measure of development'. With the growth of the industrial society, the accompanying innovations in technology, and the need for its management, professional attributes will interact with needs of the organization and influence its goals and policies, thus creating symbiotic growth for both.

Over time, professionalism and professional behavior became more of an individual attribute divorced from the context within which professionals operated. In 1968, Hall described the attitudinal attributes of professionalism as,

> "A belief in the service to the public- this component includes the view that the work performed benefits the public primarily, a sense of calling to the field- this reflects the dedication of the professional to his work and the feeling that he would probably want to do work even if few extrinsic rewards were available. Autonomy- this involves the feeling that the practitioner ought to be able to make his own decisions without external pressures from client, those who are not members of his profession, or from his employing organization" (Hall, 1968).

This attitudinal view of professional behavior has persisted over time as evinced by a survey of professional school faculty and professionals by Hall and Berardino where the surveyed sample views professional behavior as consisting of "honesty, ethics, joining professional organization, taking independent decisions and maintaining public trust" (2006; pg 408). The

stability of an attitudinal view of professionalism is surprising given that attention to this subject in the academic literature has gradually increased over a period of time. A search in the database Academic Search Premier using 'professionalism' as keyword (limiters: title and abstract, peer reviewed journals and articles) resulted in a list of one thousand four hundred and twenty two articles from 1972 onwards. On mapping the frequency over time, it appears that this topic has been gaining increasing attention and experienced an upsurge in 2000-2001, which continues to date.

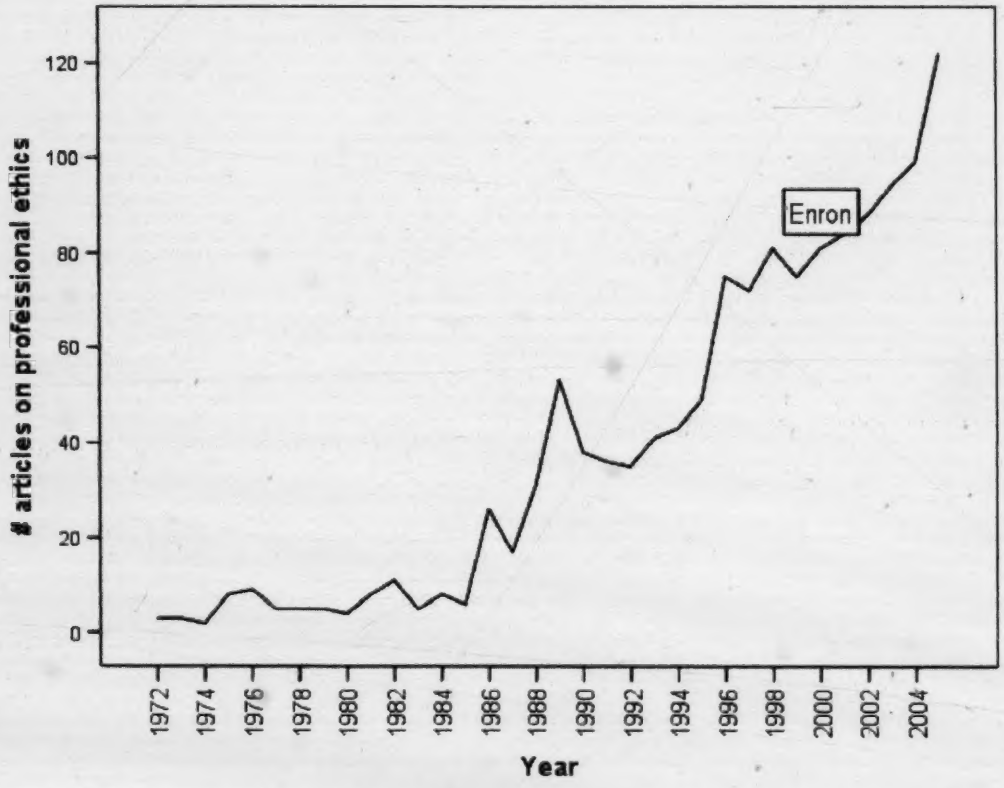

Figure 1B
Number of articles on Professionalism (1972-2005)

Much of this literature focuses on issues around the code of ethics in different professions: creating codes for quasi-professions; the problems of and existence of mechanisms (or the lack of) for enforcing; and modifying codes to reflect changing rules/regulations. Until recently, one of the dominant ways to address professional misbehavior in the literature has

been to suggest changes to the code of ethics and expect individual professionals to respect it. In other words, it puts the responsibility of professional behavior onto the initial source of socialization- the professional association. The role of the employing organization, especially professional organizations, in influencing professional behavior has generally been left under-examined.

Corporations have failed on a fairly consistent basis, and top management avarice is nothing new to research, as the literature on agency theory evinces (Jensen & Meckling, 1976; Fama; 1980). What has been different in the case of corporate failures such as Enron is the active implication of professionals (i.e., auditors, lawyers, bankers and analysts) working in large and reputable professional organizations. These large organizations exert a profound influence in the institutional fabric of global activity. Large law firms broker complex commercial activities and help to establish and then interpret the rules of the game of the capital market. Consulting firms are sources and champions of ideas about management and significant influences on how corporations are managed. Accounting firms underpin the integrity of the financial markets (Greenwood, Suddaby & McDougald, 2006).

Given the extent of influence and significance of professionals' roles in maintaining and sustaining the 'vital base of trust' in capital markets, the spate of corporate scandals involving large professional service firms has been disturbing. The issue of breach of fiduciary trust has not only been confined only to the accounting firms, but has also involved law firms, investment banks, and financial analysts. The fall of Enron along with Arthur Andersen's dissolution and the culpability of investment banks, analysts and law firms associated with it, did not end in 2002. Despite new regulations, policies and monitoring mechanisms, there are new concerns raised about these professional organizations which make it important to consider their 'dark side'. Table 1.1 provides some examples of the professional organizations under investigation since 2002.

Table 1-1: Current investigations and scandals involving large professional organizations.

Year	Professional Organization
2005	The New York Stock Exchange imposed a $19 million fine on Morgan Stanley for alleged regulatory and supervisory lapses
	A Florida jury found that Morgan Stanley did in fact fail to give adequate information about Sunbeam thereby defrauding and causing damages of $604 million. To that $604 million was added punitive damages by the jury for a total of compensatory and punitive damages of $1.450 billion.
	The Securities and Exchange Commission announced the filing in federal district court of separate settled civil injunctive actions against Goldman, Sachs & Co. (Goldman Sachs) relating to the firms' allocations of stock to institutional customers in initial public offerings (IPOs) underwritten by the firms during 1999 and 2000
2004	The Securities and Exchange Commission, NASD and the New York Stock Exchange announced…enforcement proceedings against Edward D. Jones & Co., L.P., a registered broker-dealer headquartered in St. Louis, Missouri. According to the announcement, "Edward Jones failed to adequately disclose revenue sharing payments that it received from a select group of mutual fund families that Edward Jones recommended to its customers." The company agreed to pay $75 million in disgorgement and civil penalties.
	Citigroup was also accused of helping Enron and other companies hide their losses by loaning money to those companies in a special way that would reduce liabilities visible on the balance sheet. In May 2004 the company agreed to pay $2.65 billion, or $1.64 billion after tax, to settle a class action lawsuit brought on behalf of purchasers of WorldCom securities.
	Ernst & Young has been accused of 'systematically undermining' the Sarbanes-Oxley Act, by advising clients to exploit a loophole in the law, which allows directors to bypass the audit committee by pre-approving non-audit work.
	Ernst & Young, the New York-based accounting and auditing giant, is being examined about individual tax shelters which essentially allow an executive to defer taxes on capital gains profits from the exercise of stock options. It is expected that Ernst & Young, much like Arthur Andersen, may be lined up to take the first, and perhaps most pricey, hit from both the IRS and clients
	KPMG, one of the largest accounting firms, promoted dubious charitable deductions and complicated transactions to generate phony paper losses for clients, say Senate investigators who spent a year unwinding four tax

2003	products that KPMG sold to more than 350 individuals in the late 1990s and early 2000s. The firm says it no longer offers the tax strategies. The four shelters once sold by KPMG will be scrutinized by the Senate Governmental Affairs investigations subcommittee. Meanwhile, a senior manager of KPMG is suing the firm for putting him on administrative leave after he refused to sign off on allegedly illegal tax shelters sold to an audit client
	One top Houston law firm is being sued by former Enron shareholders who charge that it approved the legality of improper deals. A court-appointed examiner in Enron's bankruptcy is probing the role of more than 40 law firms in the corporation's demise.
	Deloitte Touche Bermuda is accused of aiding and abetting the Manhattan Investment Fund's alleged $400 million fraud through audits it conducted for the 1996 and 1997 fiscal years
	Every major US investment bank, including Merrill Lynch, Goldman Sachs, Morgan Stanley, Citigroup, Credit Suisse First Boston, Lehman Brothers Holdings, J.P. Morgan Chase, UBS Warburg, and U.S. Bancorp Piper Jaffray, were found to have aided and abetted efforts to defraud investors. The firms were fined a total of $1.4 billion dollars by the SEC, triggering the creation of a Global Research Analyst Settlement Fund

The above examples are but a small sample of the instances where large professional firms have facilitated the unethical behavior underpinning these events. Much of the explanation and rationalizing of such actions is built around the 'rotten apple approach': a few corrupt professionals; or a rogue PSF, that endangers the reputation of others (Schneider, 1983). These dispositional explanations are always comforting because they suggest that there is nothing fundamentally wrong with the world; however, the regularity with which these scandals surface highlights the need to look at a bigger picture (Gunz & Gunz, 2006). This picture should focus on the varying environments of professionals in the PSFs - taking into account changes in the economic and institutional context (Cooper & Vaughan, 2005) - and examine the manner in which such changes influence professional behavior.

Interestingly, a large and influential body of work examines the adverse consequences on professionalism for professionals working in traditional bureaucratic set up. Much of this literature suggests that professional organizations are more likely to be 'professional friendly'.

The large professional organizations associated with Enron such as Arthur Andersen, Citigroup, Vinson & Elkins, and a majority of the professional organizations mentioned in Table 1.1, were dominated, managed, and controlled by professionals and hence expected to protect professional values. Yet contrary to expectations, the only expression of professional behavior during the Enron-Andersen debacle came from professionals in Enron. This is an organizational setting where research suggests professionals experience most pressure to conform. The failure to uphold professional values in 'professional' organizations underscores the need to re-initiate a discussion about the interaction between different organizational forms where professionals work and professionalism. There is a need to move beyond the focus on a code of ethics and examine in more detail the variables that directly affect professional work and behavior: employing organizations and client relationships.

The next section provides a brief overview of the literature that is discussed in detail in Chapters 2 and 5.

Professionals and Organizations

Increases in the number of professionals who work in different organizational forms such as bureaucracies, large corporations, and non-government organizations and research institutions, have led to an emergence of studies focusing on how professionals react to organizations. Existing literature continues to find the study of professionals and organizations interesting. Within this literature there are three discernable streams. The first stream highlights the incompatibility between professional norms and values and bureaucratic organizations. This stream is labeled as the 'Organizational-Professional Conflict (OPC)' (Scott, 1965; Kornhauser, 1966; Hall, 1966). A second stream, labeled the 'proletarianization thesis' suggests that professionals end up subordinating their professional values to organizational goals and imperatives (Sorensen & Sorensen, 1974; Derber, 1982; Freidson, 1984). The third stream, labeled the 'adaptation thesis' (Wallace, 1995) suggests that organizations manage professionals by structuring departments attuned to professional values and norms.

All three research streams coalesce around the view that organizational forms higher in formalization impede professional behavior. Bureaucracies that emphasize standardized ways of managing work, centralized systems and clearly separated organizational roles are seen as restricting traditional conceptions of professional behavior such as self regulation peer review and autonomy. Organizational forms that are owned and managed by professionals, such as autonomous professional organizations (i.e., professional service firms) and are low in formal structures are considered more 'professional friendly'.

The focus on formal structures leads to two weaknesses. First, it tends to neglect factors within and outside of an organization that may influence professional work. Second, in setting up autonomous professional organizations as nurturing professional values, it ignores the variety of organizational arrangements that exist within this group. The rapid growth in size and service offering and geographic expansion have forced large professional organizations to devise governance structures to balance the tension between the pressures of economic performance and professional obligations and those between professional autonomy and bureaucratic control (Greenwood, Suddaby & McDougald, 2006). These tensions are likely to influence professional behavior in distinctive ways and thus warrant more research.

The above discussion emphasizes the importance of revisiting the issue of professionals and organizations for two reasons. First, it is essential to acknowledge the variety of organizational forms that professionals work in. Second, there is a need to examine the manner in which different organizational forms influence professionals' conceptions of their roles and responsibilities, thus helping us understand better how professionals negotiate organizational and professional conflicts.

Professional-client Relationships

One of the most important variables affecting professional work and subsequent behavior is the relationship between the professional and the client. The recent corporate scandals including Enron and WorldCom were disturbing for various reasons: the failure of professional gate-keepers to heed the warning signs; the avarice of the top management; and most disturbing, the evidence that the professionals in the law firms, accounting firms and investment banks *actively* colluded with top management, and in some cases with each-other, to create and obfuscate sophisticated but fraudulent financial instruments.

As the range of professional work settings has expanded, so has interest in professional-client relationships. Studies in this area have moved beyond the image of a sole professional interacting with a lay client, to focus more on professionals in organizations (i.e., bureaucracies or PSFs) interacting with client or client organizations. Unlike research in professionals and organizations, it is difficult to identify clear research streams in the area of professional-client relationships. Nevertheless there may be two discernable research foci. The first stream is concerned primarily with the increasing number of professionals working in organizations. It examines how features of the employing organization and the compatibility or incompatibility between professional and client characteristics affect client interaction and satisfaction. The second and more popular stream focuses on power inequity between professionals and clients. Here, studies focus on an event, find the dominant partner in the relationship and explain the outcome on the basis of power inequity. A large number of studies dealing with power inequity are based on an analysis of client characteristics and organizational characteristics (such as levels of authority and lack or predominance of bureaucratic orientation) to understand where power is concentrated (Gibbins & Wold, 1982; Lord 1992; Louwers, 1998).

Power is an important concept that helps in understanding the state of professional-client relationships. Earlier studies of professionals and clients focused on the asymmetry of knowledge that exists in this relationship (Sharma, 1998). This asymmetry enables a professional to influence and guide client action. The asymmetry of knowledge model is

applicable for lay individual clients but is less salient for large corporate clients who have their own in-house expertise and can contest the claims of professionals. Some studies have started exploring the power of large clients in influencing professional work. An example of such a concept is 'client capture' (Macy & Sale, 2004). Client capture highlights not only the power of large clients; it also reflects choices that professionals/PSFs make to accommodate client interests. This is important because unlike the power inequity theme which suggests that one partner of the dyad will exert pressure on the other to achieve a desired end, client capture suggests that the process is more accommodating of and voluntary for *both* the professional and the client's needs than previously anticipated. However, client capture is still a nascent theme and requires more detailed understanding of the processes and dynamics that constitute it.

The above discussion highlights how professional-client relationships have focused mainly on two themes: characteristics of professionals and clients and power inequity. A feature common to both streams of research is that a majority of studies are primarily quantitative in nature. This approach fails to examine how power and interests of participants affects the dynamics of this relationship. Another weakness in this literature is the tendency to concentrate on an event (i.e., an issue in auditing) to understand the professional-client relationship. While this focus helps in comprehending how organizational compatibility or power inequity plays out in a specific issue, it is not necessarily indicative of the nature of the professional-client relationship. A final weakness in the literature is the focus on studying this relationship from the perspective of the client. Little attention is given to examining the effect of changes in service content and delivery on the professionals.

In order to understand the dynamics in professional-client relationships and its effect on professional behavior, I propose to explore this relationship using a field level approach. In institutional theory, a field is defined as consisting of the totalities of relevant actors that interact more frequently and fatefully with one another than with actors outside the field (Scott, 1995). In the case of professional-client relationships, a field approach would entail a shift away from the dyad (professional-client) and necessitate a consideration of the other organizations that interact with or are affected by this relationship.

A field level perspective will also offer a more nuanced understanding of the opportunities and constraints experienced by professionals in different organizational forms when reconciling organizational goals and professional values. Examining professional-client relationships from a field level perspective offers two advantages. First, there is an opportunity to explore the processual nature of the professional-client relationship that emphasizes power and interests during negotiations. Second, a field level approach sees the professional-client relationship as part of interorganizational relationships where pressure to maintain it because of its associational advantages affects the agencies of those involved.

In summary, this thesis will be organized around two central questions:

- How does professional behavior vary across different organizational forms?
- How do professional-client relationships influence professional behavior?

The case of Enron and the PSFs associated with it is apt for examining the issue of professional behavior because it offers instances that are inconsistent with the expectations of extant literature. At the same time, this case is similar to other corporate failures where certain PSFs were seen as key contributors. Such cases highlight the importance of revisiting our understanding of the factors that influence professional work and behavior.

The central questions will be examined using the Congressional hearings related to Enron. The hearings will be analyzed using the 'textual approach' which allows for systematic assembly, presentation and interpretation of a set of related texts or documents concerning important organizational events (Gephart, 1993; Perlow & Weeks, 2002). It is also an effective means to uncover the practices or processes that generate and sustain interpretations of responsibility for actors.

This thesis document has been organized in the following manner: Chapter Two elaborates the theme of professionals and organizations by providing a detailed review of the literature and the gaps therein. Chapter Three focuses on methods: research site, data sources and the

analytic approach used in the empirical pieces. Chapter Four is an empirical piece focusing on the first research question. Chapter Five examines the literature on professional-client relationships. Chapter Six provides an overview of the analytic processes used in the second empirical piece. Chapter Seven is an empirical piece discussing the professional-client relationship. Finally, Chapter Eight discusses and concludes the thesis.

Chapter 2
Theoretical Context

This chapter reviews the research in professionals and organizations. One of the central motivations of this review is to demonstrate the limited ability of extant research to explain professional behavior in the case under consideration: Enron and the PSFs it associated with. In this chapter, I examine three research streams, highlight the merits and weaknesses of existing research, and finally outline the first research question. The rest of this Chapter is organized as follows: the first section provides a review of professional behavior. The next section offers a historical background that situates the theme of professionals and organizations within the literature on the sociology of the professions after which I offer a review of the three main research streams and their weaknesses. I then suggest using Brint's models of professionalism (1996) to understand how perception of professionalism may vary across organizational forms. Finally I address how this approach enables a better understanding of professional behavior in different organizational forms.

Professional Behavior

Professional behavior and conduct was seen and even now still largely understood as an aspect of an unwritten contract between a profession and society for the privileges of self-regulation and work autonomy. As I see it, the idea of professional behavior is a little more complicated than the issue of fulfilling societal expectations. The professional model from very early on stressed the autonomy of the individual professional to enter into relationships with clients and to conduct his/her work in accordance with his/her own discretion, guided by internalized standards and free from outside control. This model would suggest that professionals in organizations enforce their own definitions of what constitutes professional work and are independent of the organizational context in which they work (Carr-Saunders & Wilson, 1933; Moore, 1970; Johnson, 1972; Breslau, Wolf & Novack, 1978). The relationship with the public however has evolved over a period of time.

> " A profession is a vocation which one had chosen for special natural fitness and for which one has prepared by the acquisition of special knowledge, which will increase by

original contribution in order to serve society better, if possible," (R.M. Binder in Meadows, 1946).

The aspect of special knowledge and autonomy of professional work and need for discretion have been present in the earliest literature addressing professional conduct. But, the idea of serving society better is more of a suggestion. Over time service to society became one of the constituents of the professional model. Extant literature suggests that the central dimensions of a professional culture are a commitment to calling and a 'service orientation' (Moore, 1970; Rynes, 2005). Commitment to a calling involved accepting the norms of a career and identifying with the profession it represents in its collectivity. Greenwood (1957) described a professional career as a life devoted to good works wherein professional work is never viewed solely as a means to an end; it is the end itself. He stated, "it is this devotion to work that imparts to professional activity the service orientation, and the absorption in the work is not partial, but complete; it results in a total personal involvement". (1957:17)

The service orientation here is seen as a consequence of being a committed professional, not as a pre-requisite for being one. Some of the later research focused on examining the constituents of a service orientation. Moore (1970) described service orientation as a set of three related norms: rules of competence, rules of conscientious performance, and rules of loyalty or service. Competence is not just the education and credentials that lead to admission into the profession but also the maintenance and improvement of both individual and collective standards. Service was seen as a commitment to community rather than self: "the professional owes the public not only his own honorable conduct, but also, in return for the claim of collective self-control, responsibility for the discipline of wayward brethren." (1970:147). In this extract the notion of a contract between professionals and society is much more explicit; it gradually became more taken for granted and dominated other aspects of professional relationships, as the following example illustrates:

> "By certifying the public reports that collectively depict a corporation's financial status, the independent auditor assumes a public responsibility transcending any employment relationship with the client. The independent public accountant performing this special function owes ultimate allegiance to the corporation's creditors and stockholders, as well as to the investing public. This public

> watchdog function demands that the accountant maintain total independence from the client at all times and requires complete fidelity to the public trust." (Former Chief Justice Warren Burger on behalf of a unanimous Supreme Court, 1984 in Moore, Tetlock, Tanlu & Bazermann, 2006).

In the above extract, allegiance to public trust is expected to dominate all other aspects of professional work. This is a change from the initial model (Meadows, 1946) which emphasized autonomy of work, competence and discretion which would subsequently lead to service to the public. The realm of accountability for professionals expanded to include a strong consideration of an external constituent that may not be involved in the direct professional-client interaction.

Bayles (1981) identified groups affected by the activities of those who call themselves professionals as being the professionals themselves, their clients and the general public. That means that in order to understand professional behavior, we need to focus more on the relationships between professionals, clients and the public they are supposed to serve. The market mechanism controlling interactions between 'organization' and 'external claimant' can be applied to understand the nature of interactions between the professional/profession and the general public. The relationship between the professional and the client is managed by the employment contract, which would be influenced by the professional's employing organization. Finally, the intra-professional relationship is a peer relationship. Interrelationships between any of the groups must pay attention to the needs of both each other and the third group. It is the requirement to consider those who are not involved in the direct transaction that gives professional behavior its fiduciary nature, and that emphasizes the normative aspect occurring in discussions of professional conduct.

This section illustrates the manner in which the notion of professional conduct has evolved over time. It also suggests that the idea of professional conduct incorporates the expectations of a number of groups affected by the activities of the professionals (Neale, 1996). The recent scandals involving professionals can be perceived in three different ways: one reaction to the evidence of misconduct is to regard the incidents as 'symptoms'; the

cause of which is a general decline in ethical ethos. Another is to express concern that codified standards are inadequate, misunderstood or ignored, either by those enforcing or those complying with them. A third alternative is to regard both professional conduct and professional misconduct as intrinsic to the relationships surrounding a profession. Professional behavior from this perspective then is behavior that is negotiated and deemed appropriate in accordance with the groups that professionals interact with (i.e., the employing organizations, the clients and the external public). The Enron-Arthur Andersen case also illustrated that all employing organizations may not have the exact same influence on their professional workforce. While some of the in-house professionals in Enron exhibited behavior that was consistent with general expectation of accountability to an external constituent, another group of professionals from the large professional organizations garnered support for a version of professionalism grounded more in rules. This would suggest that the employing organization has an important influence on professional work and behavior. This leads to the next section, which reviews the research on professionals in organizations.

Professionals in Organizations

The study of professionals in organizations as an area of inquiry has a long research history (Gouldner, 1957; Wilesnsky, 1964; Sorensen & Sorensen, 1974; Organ & Greene, 1981; Barley & Tolbert, 1991; Wallace, 1995; Leicht & Fennel, 2001). It started first with an interest in understanding the core characteristics of professions and their interaction with organizations where increasing proportion of professionals are employed. As the sociology of professions literature evolved to map changes in professions, interest in professionals in organizations grew.

Traditionally, medicine, the ministry and law were considered to be the original professions in western societies (Carr-Saunders & Wilson, 1933). The ascension of industrialization, professional associations, salaries and levels of education transformed many diverse occupational groups into professions (Vollmer & Mills, 1966). Early approaches to studying professions focused on developing exhaustive lists of attributes designed to embody the ideal

type characteristics of emerging and current professions. Scholars such as Carr-Saunders and Wilson (1933), Marshall (1951), Goode (1957) and Greenwood (1957) came out with lists of varying lengths to identify the defining traits of professions (Scott, 2003). These traits included practice based on formal knowledge, claims for autonomy in conducting work, norms espousing a service orientation, and certification by the state.

The origins of the initial discussions of the relationship between professionals and organizations started along with the trait based approach (Hinings, 2004). In the earlier studies, organizations are seen as secondary concerns for professionals. As Carr-Saunders (1927) succinctly put it: "a man's permanent attachment is to his profession." Organizations were seen as transitory groups organized around practical ends while professions were organized around functions and hence would last much longer (Vollmer & Mills, 1966).

With the gradual increase in the proportion of professionals working in bureaucracies, studies started emerging around professionals in organizations. Blau and Scott (1962) attempted to contrast the structures of professional and bureaucratic systems in a manner that would recognize their similarities which are:

- Administration based on abstract principles
- Emphasis on expertise and specialization
- Valuing achievement versus ascription
- Affective neutrality

The differences between the two are particularly in control mechanisms. That is, professional systems place less emphasis on formalization and hierarchical control and more on socialization and collegial control.

Later studies focused on organizational forms that seemed more or less empathetic to professionals. One of the early typologies of organizational forms is offered by Scott (1965). He describes professional organizations as "organizations in which members of one or more professional groups play the central role in the achievement of the primary organizational

objectives" (Scott, 1965:51). The basis of this typology is the amount of autonomy granted to professionals by the administrative control structure, which results in two models of professional organizations:

- Autonomous professional organizations: In these organizations, professionals have considerable responsibility for defining and implementing organizational goals, for setting performance standards, and for seeing to it that standards are maintained. Individual professionals are expected to be highly skilled and motivated and to have internalized professional norms so that little external surveillance is required. In the autonomous professional organizations, a relatively clear boundary is set up between those tasks over which professionals assume responsibility and those over which administrative officials have jurisdiction. Examples of autonomous professional organizations include medical clinics, research organizations and scientific institutes.
- Heteronomous professional organization: In these organizations, professional employees are clearly subordinated to an administrative framework, and there is a relatively smaller amount of autonomy available to the professional employees. An elaborate set of rules and a system of routine supervision controls most aspects of the tasks performed by the professionals. Examples of such organizations include libraries, secondary schools, social welfare agencies, small religious colleges and firms engaged in applied research.

Other notable typologies are offered by Bucher and Stelling (1969) and Mintzberg (1979). The central focus in the work of Bucher and Stelling is on examining "what kind of an organization results when professionals are doing the work of the organization" (1969:3). Professional organizations, they suggest, are identified by two features: first, the extent to which professionals control the policies and operations of their own organization; and second, the extent to which professionals influence goal setting and policy making for the entire organization. These organizations have the some salient characteristics:

- Extensive role creation and negotiation: Professionals typically build their own role in the organization rather than fitting into preset roles. Role setting proceeds through negotiation with relevant figures in the organization.

- Spontaneous internal differentiation: The differentiation in the organization is not mandated from the top but occurs as a consequence of the building of work interests among congeries of professional workers.
- Integration through political processes: With growth, groups of professionals vie for resources and influence leading to substantial amount of bargaining and negotiation in order to accommodate varying interests. A major aim of the different groups in this process is to influence the setting of goals and policies of the organization.
- Shifting locus of power: Power in professional organizations is a fluid phenomenon not necessarily identical with office. It shifts as professionals move through the organization, and in response to different issues.

In 1979, Mintzberg came up with the concept of a professional bureaucracy, a structural configuration common in universities, general hospitals school systems, public accounting firms, social work agencies and craft production firms. The professional bureaucracy is described as an organization that:

> "...relies for coordination on the standardization of skills and its associated design parameter, training and indoctrination. It hires duly trained and indoctrinated specialists-professionals- for the operating core and gives them considerable control over their own work. In effect, the work is highly specialized in the horizontal dimension, but enlarged in the vertical one" (1979:349)

Within the professional bureaucracy, control and coordination is achieved through decentralization of authority characterized by the autonomy available to the individual professional and the standardization of skills and knowledge. The system works because "...everyone knows that everyone else knows roughly what is going on" (Meyer quoted in Weick, 1976). The standardization of skills and knowledge comes through extensive training received over a period of time in a university or a special institution. The role of the employing organization is to provide more on-the-job training and practice until the professional 'internalizes the standards that serve the clients and coordinate professional work'.

According to Mintzberg, the professional bureaucracy is different from the traditional bureaucracy in one marked way: the traditional bureaucracy generates its own standards – its technostructure designing the work standards for its operators and its line managers enforcing them. The standards of the professional bureaucracy originate 'outside its own structure', in the self governing associations. Its operators join with their colleagues from other professional bureaucracies. Whereas the traditional bureaucracy relies on the authority of a hierarchical structure and the power of office, the professional bureaucracy emphasizes authority of a professional nature – the power of expertise.

All three typologies share an important similarity: they focus on the degree of autonomy available to professionals to influence and control organizational goals. Both Scott and Mintzberg focus more on the structural aspects of the organizations. Scott's autonomous professional organizations category is similar to the characteristics of Mintzberg's professional bureaucracy: both generate their own standards; require little external surveillance; and are more influenced by professional rather than organization-specific norms. Bucher and Stelling's classification is based more on the level of flexibility rather than structural aspects. The emphasis on spontaneous internal differentiation, the ability of professionals to create and negotiate roles, and the shifting locus of power points to an organization low in formal structure that is relatively decentralized. However this is not a necessary condition. In fact, Bucher and Stelling's classification suggest a set of characteristics which if transferred within certain departments of large bureaucracies will help create a professional organization-like environment. One of the most salient characteristics of these typologies (and thus a core requirement of any professional organization) is that they are created around professional values of autonomy and peer control. This feature may have contributed to the perception of professional organizations being professional friendly, leading more studies to focus on understanding the consequences for professionals in other organizational settings.

The literature on professionals in organizations shows three distinct research streams: the Organizational Professional Conflict (OPC) thesis (Scott 1965; Hall, 1966; Kornhauser, 1967), the Proletarianization thesis (Freidson, 1974) and the Adaptation thesis (Wallace,

1985). Central to these research streams is the aim to examine if professional values can survive in organizational settings. All three streams deal with this concern in different ways. Research in the OPC stream focuses on the incompatibility between professional values and organizational goals. This incompatibility expresses itself more strongly in organizational forms such as bureaucracies. Features central to bureaucratic forms such as formalization, hierarchy and rationalization of tasks are expected to clash with professional norms of self-regulation and peer control. Such incompatibility results in professionals in bureaucratic forms experiencing strain and conflict. The Proletarianization thesis emphasizes the circumstances of professional work in large organizations (Freidson, 1984). It stems from the difference between the idealized image of an independent professional who can regulate sale of his/her service under fairly loose market conditions and professionals employed in large organizations who are not able to control the terms of their work. While the OPC thesis focuses on the conflict that is the result of opposing or divergent values, the Proletarianization thesis focuses more on the gradual loss of professional identity that takes place when professionals work in bureaucratic set ups for long periods. The last stream, Adaptation thesis, focuses more on how large organizations may accommodate their professional workforce by designing their professional departments to resemble professional organizations. The next section elaborates each of these research streams.

Organizational Professional Conflict Thesis (OPC): This research stream is one of the earliest approaches to studying professionals in organizations. It gained impetus during the 1950s and has remained a persistent theme in the literature. The conflict argument stems from an understanding that bureaucratic goals and professional values are at odds with each other and result in competing loyalties among salaried professionals (Scott, 1965; Sorensen, 1967; Miller, 1967). The assumptions that underlie this perceived conflict have to do with an idealized notion of an autonomous professional and the Weberian model of bureaucracy (Larson, 1977). As carriers of the norms and ideals of professionalism, professionals in bureaucratic organizations are expected to experience threat and contradictions. The threats derive in part from the contrast between self-regulation and peer control, characteristics of professional work and externalized control of a bureaucratic hierarchy (Vollmer & Mills, 1966).

Early writers such as Mills (1951), Lewis and Maude (1953), Merton (1957), and Whyte (1957) take a dim view of the transition of professionals to hierarchical organizations. They argue that administrative aspects 'restrict the professional's freedom' and make him dependent upon the organization. They believe that association with bureaucratic organizations prevented the professional from fulfilling a fundamental requisite of professional behavior; that is, serving the best interests of his clients and the community (Engel & Hall, 1973). Other studies in this stream highlight how professionals' work activities in bureaucratic organizations and corporations are directed toward servicing goals established by the management. Career progression within the organization tends to be dependent upon meeting these goals. Not only is the conduct of professional work in these situations subject in large measure to managerial evaluation but management also exercises substantial control over professional staffing levels and remuneration. Clashes between these antagonistic values could create potential conflict between loyalty to the organization and loyalty to the professional community, leading to heightened alienation and dissatisfaction among professionals.

Research in the OPC stream can be differentiated into two subgroups: first, a set of early studies focused primarily on the professionals working in bureaucratic organizations; and second, a set of later studies that examines professionals in autonomous professional organizations. The early set focuses on the increasing diversity of work-settings where professionals are found, and examines empirically the pessimistic forecast of the earlier writers. These studies investigate a variety of organizational settings such as public welfare departments (Scott, 1965), corporations (Taguiri, 1965; Kornhauser, 1966; Miller, 1967; Hall, 1967; Organ & Greene, 1981; Spangler & Lehman, 1982; Pei & Davis, 1989), and universities (Wilensky, 1964; Jauch, Glueck & Osborn, 1978). Most of them focus primarily on comparing structures of bureaucratic organizations to autonomous professional organizations. Some of the studies supportive of the OPC thesis found degree of formalization, hierarchy or bureaucracy as the main source of the conflict experienced by professionals, suggesting that bureaucratic organizational forms are not professional friendly settings:

> "A professional is presumably a person, who derives his aims and methods from a professional body, works independently, and who commands the privilege to autonomously determine what should be done and how it should be done. Should the professional find himself working within the confines of a formal organization, inevitable tensions and conflicts can be expected between the requirements of the bureaucratic system, and the values of the professional. Within a bureaucracy, a professional is seen as a bureaucratic functionary, whereas in fact he is independent, guided in his relationship to a client by a professional subculture and normative system" (Bucher & Stelling, 1969:13).

This research subgroup suggests that an important source of conflict for professionals is the difference in values (Taguiri, 1965) and perception (Corwin, 1961) between professionals and administrators. While several studies provided support for the OPC thesis (Corwin, 1961; Wilensky, 1964; Taguiri, 1965; Scott, 1965; Kornhauser, 1966; Miller, 1967; Engels, 1970; Organ & Green, 1981; Aranya & Lachman, 1982; Aranya & Ferris, 1984; Pei & Davis, 1989), a fair number offered mixed results and some caution. Influential among them are Hastings and Hinings (1970) and Hall (1967), both of which suggest that OPC may be related to other factors apart from organizational structures. Thus along with support for the OPC thesis there was also skepticism expressed regarding results that supposedly uncovered the anticipated discontent. The motivation behind this group of studies was primarily to examine the source of conflict in bureaucratic organizational forms. As evidence, most of the studies traced the source of conflict to presence of formal structures, the inability of professionals to control the content and process of their work and the value difference between professionals and non-professionals.

As studies focusing on professionals in bureaucratic organizations grew and found increasing support for the organizational-professional conflict thesis, the second subgroup (especially from 1980s onwards) started examining professionals in autonomous professional organizations. These studies appear to be a natural outgrowth of the research examining professionals in bureaucratic organizations because they focused on organizations where professionals would experience the least amount of strain or conflict; that is, organizations owned and controlled by professionals. This later set examined professionals in autonomous

professional organizations such as law firms and accounting firms to find that conflict or stain are minimal or even absent in such organizations (Montagna, 1969; Lengerman, 1971; Spangler & Lehman, 1982; Aranya & Lachman, 1982; Aranya & Ferris, 1984; Lachman & Aranya, 1986). Many others compared job satisfaction, organizational commitment and professional commitment of professionals working in autonomous professional organizations to those in other organizational settings such as government departments or in corporations (Strawser, Ivancevich & Lyon, 1969; Aranya, Polloack & Amernic, 1981; Aranya & Lachman, 1982; Aranya & Ferris, 1984; Lachman & Aranya, 1986). Findings of this subgroup suggest that professional and organizational commitments for professionals in autonomous professional organizations are strongly and positively related. This finding is significant because organizational and professional commitments are conceptualized as very different constructs. Studies on professionals in bureaucratic organizations found organizational and professional commitments negatively related (Jauch, Glueck, Osborn, 1978; Blein, Doucher and Meixner; 1991; Somech & Bogler, 2002). Professionals in autonomous professional organizations also have higher job satisfaction, autonomy and less strain compared to professionals in other settings (Stawser, Ivancevich & Lyon, 1969; Pei & Davis, 1989). This harmonious codependency is explained away as an outcome of fewer structures and greater autonomy in autonomous professional organizations without exploring possible effects of other organizational features.

The absence of formal structures and lack of hierarchy was seen as the primary reason for low conflict in autonomous professional organizations. In an influential study, Montagna (1968) found that while accounting firms were administered from within, their standards were set externally by the profession, rendering formal controls unnecessary. The lack of formalization became equated to congruence with professional values, leading to the notion that autonomous professional organizations are more 'professional friendly' than other organizational forms.

To study the research on the OPC stream, I used JSTOR and 'Academic Search Premier' (search engines) with peer reviewed business and sociology journals as limiters. The journals included *The Academy of Management; Academy of Management Review; Administrative Science*

Quarterly; Accounting review; Journal of Accounting Research; Accounting, Organizations and Society; Journal of Business; ,Journal of Human Resource; Journal of Law, Economics and Organization; Journal of Organizational Behavior; American Journal of Sociology, American Sociological Review, Annual Review of Sociology; Law and Society Review; Sociological Theory; and Theory and Society . The search yielded a total of eight hundred and thirty four articles. These articles included theoretical discussion and empirical pieces that examined conflict related to gender, ethnicity, economic background and various occupation groups. I refined the search further to focus on empirical articles related to the professions which narrowed the total number to one hundred and thirty seven articles. Out of the total, one hundred and three articles provided strong or moderate support for the OPC thesis, while thirty four did not find OPC effects. Table 2.1 provides a selected sample of twenty studies out of which yielded sixteen that were supportive of the thesis that professionals experience strain (Wilensky, 1964; Scott, 1965; Kornhauser, 1966; Organ & Greene, 1981), alienation (Miller, 1967; Schrroeder & Imdieke, 1977) and loss of autonomy (Engels, 1970; Lengerman, 1971; Spangler & Lehman, 1982) in bureaucratic organizations.

In sum, research in the OPC stream generally provides support for two ideas; first, professionals are different from other organizational members, that is, they are part of a community that shares a common definition of professionalism; and second, that bureaucratic organizations impede professional work and conflict with professional values while others such as autonomous professional organizations are more professional friendly. The next stream of research has a slightly different orientation. Similar to the OPC thesis it continued to focus on professionals in bureaucratic organizations, but also examined the consequences of staying on with such organizations for professionals.

Proletarianization Thesis: This line of research continues to build on the theme of professionals as a distinct community but focuses more on the transformational threats that professionals in bureaucracies or non-professional organizations face. An important motivation for this research steam is distinguishing between characteristics of professionals and bureaucrats to highlight the enormous (and implicitly, disastrous) transformation that would take place if

professionals continue to work within bureaucratic organizations for a long time. Ness (1986) elaborates the difference between professionals and bureaucrats:

> "...a professional's credentials are a form of property that plays a major role in the sense of identity-their entire conception of who they are. As bureaucrats, they may never appropriate their office, and must absolutely separate their private life from the position in the bureaucracy. Professionals set their own goals, based on their professional socialization. As bureaucrats, they tend to be isolated from the goal setting process and make decisions based on the requirements of their office...the ultimate justification of a professional act is that it is, to the best of the professional's knowledge, the act which best meets the professional's goals. The ultimate justification for a bureaucratic act, however, is that it is in line with the organization's rules and regulations and that it has been approved by a superior rank. A professional can generally choose his own client, but as a bureaucrat he must accept any clients provided to him by the rules of the organization. Finally there are many 'free professionals', but there are no free bureaucrats" (1986:64).

Unlike the OPC stream which focuses on the strain and conflict that professionals face in bureaucratic organizations that leads to their higher turnover, the proletarianization thesis entertains the possibility that professionals may survive and even thrive in bureaucracies. It is the threat of long term change that concerns this stream of research: the loss of control over professional work and output; the change in orientation from valuing autonomy to being subservient to authority; and the distance from the professional community.

Similar to the research in the OPC stream, the proletarianization thesis suggests that organizational structures are necessarily oppressive of the professional spirit (Cohen, Finn, Wilkinson & Arnold, 2002). However, it focuses more on the consequences of employment for professionals. Employment is an important factor for professionals because it implies losing the capacity to control terms of their work (Freidson, 1984). Changing employment patterns also have important effects on the life chances of professionals. Employment opportunities may be rearranging the structure and aspirations of professional careers (Calhoun, 1965). An interesting study considers the case law associates in two different

settings: first; at a large corporate law firm; second, at an office of a bureaucratized mass market seller of legal services. Both groups work long hours, have little control over what they work on, must have their work approved by a hierarchy of colleagues and can be described as cogs in a large division of labor. But here Rosen (1999) points out the critical difference:

> "Yet there is a significant difference, is there not? One difference is in their careers. The corporate law firm associate can dream of a career that leads to a professional ideal, symbolized by an understanding of partnership. Promotion for the other, if possible, is only onto management ranks, not to a different relation of control over legal work. For this reason, this associate might be described as deprofessionalized" (Rosen, 1999:704)

Thus, at the foundation of the proletarianization thesis is the issue of power or control - the ability to determine what work is to be done, how the work is to be done and what its aim is to be. In an organizational form such as a bureaucracy where tasks are assigned rationally and ordered by hierarchical supervision, professionals are no longer able to govern themselves by their own methods of peer influence and informal control:

> "...they (professionals) neither control the production process, whose object specifications and methods are determined from above , nor their own work, which is defined rigidly within their occupational hierarchy" (Aronowitz, 1974:305).

Professionals in these organizations are managed by non-professional administrators and subordinated to an authority system that is bureaucratically driven rather than professionally driven, thus there is a higher probability of professional roles being undermined. This phenomenon is seen more vividly in organizations such as the military. In a study focusing on psychiatrists in the military, Daniels (1969) showed how it is the military, not the psychiatric profession, that defines who needs help. And it is the military, not the client, that decides how much of the psychiatric evaluations to accept. When professional access and work is mediated through a strong organization, transformation and subordination of professional behavior to organizational goals occurs. Therefore once professionals become

employees, they eventually lose that sense of autonomy that marks them out from other groups and they are essentially reduced to wage earners who are subject to forms of control that inevitably erode their status and privilege (Derber, 1982).

In sum, the proletarianization literature speaks of the general change in orientation that happens when professionals work in large organizations for a long period of time. It sees change in orientation as a natural progression. The search for articles on the proletarianization thesis yielded one hundred and twenty two studies, out of which thirty seven focused on professions. Out of the thirty seven studies, twenty two supported the proletarianization thesis, ten were ambivalent, and five clearly did not find any support. Table 2.2 presents a sample of twenty studies. Studies in this stream suggest that over time, the orientation of professionals in a large organization is replaced by an organizational orientation dominated by administrative norms (Sorensen, 1965; Ritzer & Walzak, 1988). In some cases a change is often voluntary, especially for professionals who see the employing organization as a source for achieving success in administrative positions (Derber; 1983). Where rewards are high enough, professionals may adapt their own professional ideas of competence, rewards and status to the value system of the organization they serve (Sorensen & Sorensen, 1974; Goldner & Ritti, 1967; Lachman & Aranya, 1986; Hagan, Huxter & Parker, 1988).

The key difference between OPC and proletarianization thesis is that OPC emphasizes conflict and focuses on finding the source of conflict and its relationship to turnover intention, job satisfaction and organizational commitment. The proletarianization thesis, on the other hand, focuses much more on the consequences of professionals working in a large organization. In particular, it focuses on the idea that professionals working in large organizations for a long period of time gradually let organizational concerns dominate their professional values, i.e., professionals get proletarianized. The OPC and proletarianization theses are similar in three ways. First, research in both streams gives the impression that organizations with higher degrees of formalization and hierarchy conflict with professional values. Second, both streams continue to view professionals as subscribing to a model of professionalism that remains unaffected regardless of the organizational forms where professionals work. Finally, both OPC and the proletarianization theses underemphasize professionals' ability to influence their work.

The Adaptation Thesis: A third stream of research in this area focuses more on the manner in which bureaucratic organizations attempt to accommodate professional work. In a study that compared organizational and professional commitments in law firms and law departments in corporate organizations, Wallace (1995) came up with the term 'adaptation thesis' to emphasize that all bureaucratic organizations where professionals are employed do not undermine professional values and work. Adaptation thesis can be seen primarily as a reaction against OPC and proletarianization theses, both of which highlight the problems professionals have working in some organizational forms. Research in the adaptation thesis reflects an increased awareness on the part of employing organizations about the uniqueness of their professional workforce. Studies in this stream suggest that instead of having dissatisfied professionals experiencing role strain, some organizations attend to professional concerns as much as professional organizations (Wallace, 1995). In her study, Wallace (1995) points out that most professionals in non-professional organizations work in departments that are clearly separate from the employing firm's hierarchical structure. Although salaried professionals must serve the employer's goal, which limits their freedom to some degree, they do have more autonomy, in terms of discretion and control over the performance of their professional work tasks, than previously anticipated. But it is still not comparable to the autonomy of professionals in professional organizations. This line of research suggests that structural arrangements in non-professional organizations may be more consistent with those in professional organizations than the proletarianization thesis suggests (Nelson & Trubek, 1992; Derber & Schwartz, 1991; Wallace, 1995).

Although use of the term 'adaptation' is relatively recent, studies as early as the 1960s (La Porte, 1962; Vollmer, 1966) examined how role strain in professionals could be resolved. In examining the studies on adaptation thesis, I encountered a problem with classification. As the term 'adaptation thesis' is fairly recent, articles that have explicitly used this framework are limited. Table 2.3 offers nine examples of studies that focus on adaptation thesis. Most of these studies enumerate ways in which employing organizations create different arrangements for their professional workforce. For example, in a study that focused on a variety of professionals working in large organizations, Derber and Schwartz (1991) found that departments where professionals dominate have an environment similar to that of autonomous professional firms. They called such departments 'logofirms'. For professionals

working in bureaucracies or corporations, the internal logofirm becomes a secure institutional defense against proletarianization. Other studies too, lay emphasis on the creation of separate or modified arrangements for professionals. Separation of major functional roles within the employing organization (La Porte, 1965), reduced bureaucracy (Vollmer, 1966) and environments low in control (Abernathy & Stoelwinder, 1995) are suggested as ways to better accommodate professional workforce. Some studies emphasize designing governance mechanisms that value both professional norms and organizational goals. In comparing law departments in large corporations to law firms, Wallace (1995) highlights the importance of autonomy and reward policies as two key mechanisms that create a professional friendly environment. Similarly Stern and Barley (1991) highlight the importance of having promotion criteria based on collegial structures and peer evaluation for professionals in non-professional organizations.

The adaptation thesis is different from the OPC and proletarianization theses in one key way. It goes beyond the assumption that bureaucratic settings are necessarily unfriendly to professionals. Studies in this stream highlight organizational arrangements and governance mechanisms that create a favorable environment for professional work. The results, however, are offered with two key reservations. First, despite these arrangements, internal departments or logofirms do not equal the professional friendly environment of autonomous professional organizations (Wallace, 1995). Second, though internal departments can be designed to accommodate professionals better, "such melding of apparently contradictory identities (i.e. organizational and professional) may not be stable over the long run" (Derber & Schwartz, 1991). The difference between the adaptation thesis and the OPC and the proletarianization theses then is more in the degree of support that the adaptation thesis offers for bureaucratic forms (i.e. studies in the adaptation thesis agree to a lesser extent that bureaucratic organizational forms conflict with professional norms: (Figure 2A). The adaptation thesis is similar to the OPC and the proletarianization theses in two ways: first, it persists in seeing professionals as a community sharing a common definition of professionalism; and second, it views professionals as inactive recipients of organizational action. Although the studies highlight how a more favorable environment could be created for professionals in large organizations, the focus is still on mechanisms such as role differentiation and reduced formalization.

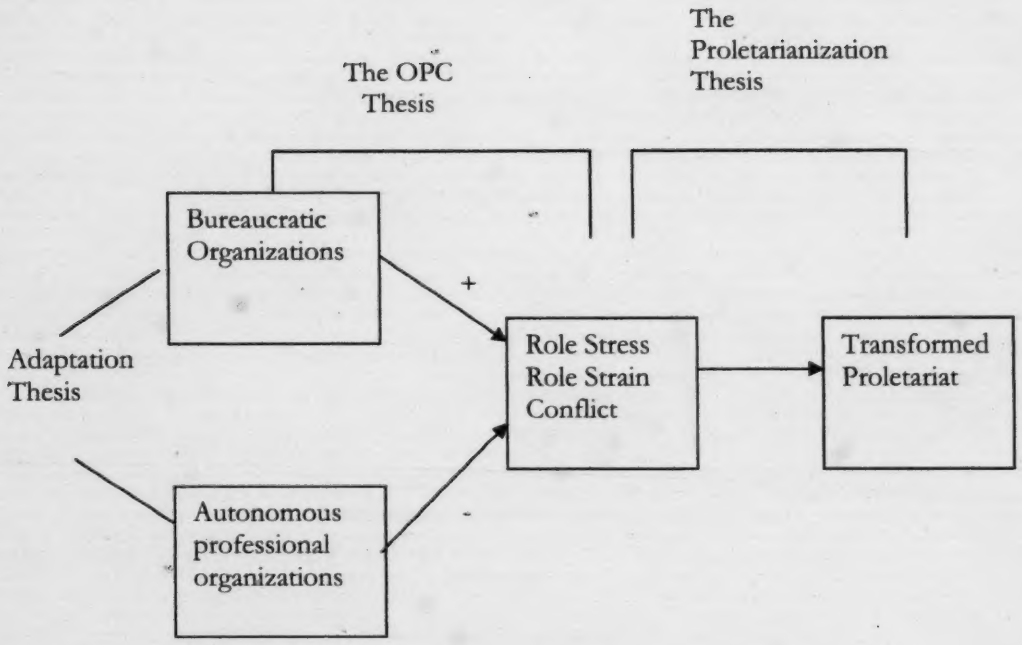

Figure 2A
The Three Research Streams in Professionals in Organizations

All three research streams have contributed in understanding the manner in which organizational settings may influence professional work and values. But Enron and the other corporate scandals involving professionals prove to be exceptions to the insights generated by this body of research. For example, based on the OPC stream, we would expect accounting and law firms to be nurturing of professional concerns. One would expect that professionals in profession-friendly organizational forms, such as PSFs are more likely to manifest professional behaviors such as conveying their objections to colleagues and seniors, internal whistle blowing, and being vocal about their responsibility to the large investing public. The case however suggests that Arthur Andersen and Vinson & Elkins were conspicuously lacking in all of the above markers of professional behavior. Similarly, based on the proletarianization thesis, we would have little expectation of professional behavior from the in-house accountants and attorneys at Enron. In fact, this was the only group of professionals that consistently protested against the management's activities. The subsequent investigations into some of the Big Four accounting firms strengthen the need to revisit the issue of professionals in organizations.

Problems in the Literature

A review of the literature on professionals in organizations points to two weaknesses: first, by focusing primarily on degree of formalization, other factors within and outside of an employing organization that impact professional work are ignored. A focus on formal structures sets up professional organizations collectively as 'professional friendly' but ignores the variety of organizational types that exist within this group. Second, by continuing to examine professionalism using criteria that remains unaffected regardless of the variety of organizational settings, the literature fails to take account of professionals' capacity to *negotiate* professional responsibility.

Formalization, Autonomous Professional Organizations and Professional Behavior: Studies in all three research streams focus heavily on the degree of formalization and hierarchy in an organization, leading to a major limitation: In setting up professional organizations as organizational forms that nurture professional values, the variety of organizational types that exist in this group are ignored. Autonomous professional organizations have changed in size, scope and complexity. The collegial arrangements of traditional autonomous professional organizations have been replaced by more managerial corporatist form as firms have responded to the pressures of size and organizational complexity (Cooper, Hinings, Greenwood, Brown, 1996). The changes mean that there are greater varieties of organizational forms used by autonomous professional organizations. It is unlikely that all of these forms will equally nurture professional norms: there will be variations in the negotiated order. The Enron, Andersen affair and the recent investigations involving large autonomous professional organizations clearly indicate the dissonance between professionals' *[illegible]eption* and the public's *expectation* of professional behavior, suggesting that there may be different conceptions of professionalism and they may vary based on organizational forms.

A non-negotiable model of professionalism- The second weakness common across the streams is that they assume that professionals subscribe to a model of professional conduct that is non negotiable, i.e. a professional not following a particular model of professional conduct will not be 'really' professional. Research in the proletarianization thesis helped strengthen the idea that professionals in bureaucratic organizations end up marginalizing professional

values. Up until the 1990s, professionalism continued to be evaluated on the criteria of: desire for autonomy; belief in self-regulation; sense of calling to the field; and belief in service to the public (Meixner & Bline, 1989; Goetz Jr., Marrow, & McElroy, 1991; Pei & Davis, 1992).

The focus on a dominant model of professional behavior also ignores factors within and outside of an organization that affect professional work and eventually behavior. For example, changes in an employing organization's resource environment affect the extent to which professionals control their work content and process. Bacharach, Bamberger and Conley (1991) suggest that munificence and scarcity of the resource environment influences the leveraging power of professionals and administrators. In times of munificence professionals in an organization have greater influence on organizational preferences, while scarcity increases the administrators' leverage. In other words, access to resources may influence the manner in which professional behavior is perceived. Similarly socialization processes, which are unique to employing organizations, can impact professionals' perception of autonomy. Socialization can be defined as the process by which individuals are molded by the society in which they seek full membership (Fogarty, 1992). It stresses the primacy of interests of the collective over those of individuals. The socialization of new members is crucial for the continuance of an existing institutional order and is undertaken by those who have the greatest stake in maintaining the status quo (Powell, 1998). Now resource environments and socialization processes can vary based on the size and service offering an even geographic location of organizations, making professional behavior much more of a *negotiated* concept than previously acknowledged.

The presence of the different organizational forms and variations in resource environments is evident especially within professional service firms, an organizational form resembling autonomous professional organizations. A professional service firm has a primary resource and workforce of a group of trained professionals who have agreed to work under the same organizational umbrella. An important characteristic of such firms is that these professionals agree to share ownership and authority which is a key defining characteristic (Hinings, Brown & Greenwood, 1991). Size distinctions within PSFs indicate substantive differences in their resource environments and the possible influence on professional work and

behavior. Professionals, especially in large professional service firms, face increasingly turbulent and complex environment because of deregulation and competition, technological development and globalization of services (Powell, Brock & Hinings, 1999). This kind of change and uncertainty alters the playing field for professionals and may affect the way they envisage their roles and responsibilities.

In addition, the size of a PSF also affects its relationship with the professional association- the traditional vanguard of the professional maintenance project (Freidson, 1994, Greenwood & McDougald, 2004). For example, smaller PSFs have limited service offerings and limited resources; they continue to depend on the professional association to socialize their professional workforce. Similarly, for professionals working in government organizations and corporate bureaucracies, the professional association continues to be the key resource for professional socialization and maintenance of standards. Large PSFs on the other hand, offer a much wider variety of specialized services. They have the expertise and the resource to develop their own training and development programs. In doing so, large PSFs are more likely to get distanced from the professional community.

One of the rarer studies (the other being Johnson, 1967) that takes into account the changing environment within which professionals work and relates it to changing models of professional behavior, is Brint (1996). In fact Brint suggests that there are at least two models of professionalism: the *social trustee model* and the *expertise based model.* The social trustee model came into prominence during the formative period of the professions. This model of professional behavior links command of an esoteric body of knowledge with wider social purposes, subordinating self-interest and commercial gains in favor of ideals of public service. The social trustee model was effective in procuring for emerging professions, privileges of self-regulation and monopoly of practice. In the 1960s there was a removal of restrictions on standard fees for service, competitive bidding and advertising. With increased competition for services and clients, a rival model of professionalism became dominant: the expertise model of professionalism. In this model, claims to professional status are predicated upon a command of an abstract body of knowledge that is superior to others in its application to a given set of activities and tasks, which is allotted through mechanisms of the marketplace. Notions of disinterested service and commitment to broader ideals of

public welfare are minimized. The presence of two variants of professionalism suggests that professionals in different organizational forms may be partial to a certain model if it is consonant with their organizational goals.

Professionals in all organizations have to reconcile two kinds of pressures: commercial pressures of revenue generation and organizational survival and expectations of professional behavior. However, large PSFs operate in very competitive environments. The pressure for greater efficiency and accountability in costs forces them to reconcile commercial aspirations along with expectations of being a 'public watchdog': a function that demands professionals to demonstrate ultimate allegiance to public trust. (Moore, Tetlock, Tanlu & Bazerman, 2006). This pressure may make the expertise-based model especially attractive for these organizations. Within the expertise model, command over an esoteric knowledge base can be translated as technical superiority, which earns credibility in its ability to achieve a desired end (Koehen, 1996). A public service ethos gets morphed into a client-focused orientation. Thus the demonstration of technical expertise in achieving a client desired end consolidates a PSF's reputation as an expert and ensures its commercial survival. Professionals in the corporate bureaucratic form also experience commercial pressure, but unlike professionals in the PSFs are not solely responsible for their organization's continuance. Their organization, however, consists of a large number of non-professionals. The social trustee model may be more attractive for them because it emphasizes values and goals that enable professionals to appear different from their non-professional colleagues.

The above discussion suggests that though all professionals face pressures to reconcile commercial concerns with professional norms, professionals in corporate bureaucracies are different because they are not solely responsible for the survival of their organization. Professionals in large PSFs are solely responsible for their organization's survival and are much more likely to be partial to a model that enables them to pursue their commercial aspirations. The possibility that organizational forms vary in their ability to accommodate certain professional models, gives rise to an interesting question:

How does professional behavior vary across different organizational forms?

The above will be the central research question in the first empirical piece. This chapter highlights the need to acknowledge that professionals work in a variety of organizational forms that may endorse different models of professionalism. The interaction between organizational form and the endorsed models of professionalism influences professional behavior. The next chapter provides an overview of the professional-client literature.

Table 2-1: Examples of Studies Focusing on Organizational Professional Conflict Thesis

No	Study	Data	Purpose	Result
1	Corwin (1961)	296 graduate and student nurses	Analyzing the discrepancies between ideal perceptions of role and its reality of nurses with graduate degrees and with diplomas	1. Highest level of OPC present at graduation 2. Academic degrees and professional orientation are positively and strongly related. 3. Higher the professional orientation, greater the OPC conflict.
2	Taguiri (1965)	Scientists in industrial organizations, executives and managers of research personnel	Comparative study of the values held by scientists in industry, by executives and by managers of research personnel.	1. Significant levels of conflict and alienation present for scientists. 2. Scientists very high on professional orientation and low on organizational orientation 3. Administrators high on organizational orientation. 4. Conflict attributed to difference in values of the two groups.
3.	Scott (1965)	Differentiated between autonomous and heteronomous organizations. Looked at professional workers in the largest two divisions of a public welfare agency (heteronomous organization).	Study the reactions of professionals to the agency's system of routine supervision and how it impinges on the individual professional worker.	Professionals in heteronmous organizations experience more conflict than those in autonomous organizations. 1. Professionals in heteronomous professional organizations felt their functions constrained by administrative and legal framework. 2. Professionally oriented workers were more critical of the system than nonprofessionally oriented workers. 3. Workers supervised by professionally oriented supervisors were less critical of the system than workers serving under less professionally oriented supervisors.

5	Miller 1967	Compared scientists and engineers in two research divisions of a very large organization. One that was more autonomous and the other that had more formalization built in.	Relationship between alienation from work and two dimensions of organizational structure are explored.	1. Alienation from work is a consequence of the professional-bureaucratic dilemma for engineers and scientists. 2. Alienation was strongly associated with type of supervisor and degree of organizational encouragement for more professionalized group.
6	Hall (1967)	Compared autonomous, heteronomous and other organizations (data gathered from 23 organizations- e.g. 6 groups of lawyers distributed between a medium sized law firm, a small unit of department in the federal government and legal departments of private corporations)	Examine the organizational bases of professional organizational relationship	1. On hierarchy of authority dimension- Autonomous organizations are significantly less bureaucratic than the other two types of occupational groupings. 2. On the division of labor dimension- autonomous organizations are much less bureaucratic than heteronomous and departments. 3. On the presence of rules- autonomous organizations characterized by fewer rules, followed by professional departments and heteronomous organization.
7	Engels, 1970	Compared three groups of physicians- solo practitioners (non bureaucratic), a privately owned closed panel medical organization (moderately bureaucratic) and a government-associated organization (highly bureaucratic).	Exploring how bureaucracy affects professional autonomy. Independent variable- degree of bureaucracy and dependent variable- degree of professional autonomy.	1. A greater percentage of physicians in the moderately bureaucratic settings perceived themselves as high in autonomy than in either of the two settings 2. A greater percentage of those in the highly bureaucratic settings perceived themselves as low in autonomy. 3. Professionals in solo practice were more involved with professional activities. 4. Suggests degree of bureaucratization more important than just a focus on structures.

8	Lengermann (1971)	373 CPAs in different types of work locations-solo practice office, local firm, regional firm, national firm and non-CPA organization.	Take a descriptive and empirical look at the relative levels of professional autonomy enjoyed by CPAs in the different types and sizes of CPA work situations.	1. The opportunity for professional autonomy is greater for CPAs in the large CPA firms than for CPAs in non-CPA organizations. 2. Professional autonomy enjoyed by CPAs in CPA firms is very positively related to their position level in the firm.
9	Jauch, Glueck and Osbom (1978)	84 professors at a large Midwestern University	Examined the relationship between organizational loyalty, professional commitment and research productivity	1. Organizational loyalty and professional commitment are independent. 2. Professional commitment is positively associated with productivity and more important for job satisfaction.
10	Organ and Greene 1981	247 scientists and engineers employed in the research, development and engineering divisions of three firms. The R&D divisions of the three firms were very similarly organized- decentralized and autonomous relative to other divisions	Explores the possible compensatory effects of structural formalization in the conflict between organizational imperatives and professional norms. Dependent variable-alienation. Independent variable-formalization. Mediating variables-organizational identity, role conflict and role ambiguity.	1. Professionalization and formalization are inversely related. 2. In more professionalized groups formalization activates role conflict. This conflict fosters alienation. 3. For less professionalized groups formalization helps define organizational expectations and avenues of influence.

11	Spangler and Lehman (1982)	Studied lawyers working in large law firms, as corporate counsel and in the government.	Examining the autonomy of lawyers in relation to different organizational settings.	1. For lawyers in large law firms day to day work on cases or deals allows for a high degree of autonomy. 2. Lawyers who work as in house counsel face more pronounced and direct bureaucratization. The corporate counsel is less significant to his/her organizational employer. The nature of work that in house counsel deals with is more routine. 3. Government lawyers work in the most starkly bureaucratized work settings, but they develop expertise and experience in an area at a much faster pace. They use these appointments as an apprenticeship in the hope of attracting offers from large law firms.
12	Aranya and Lachman (1982)	Partners and sole practitioners in professional organizations (accounting firms), employees in professional organization and employees in bureaucratic organizations.	Paper focuses on the formulation and examination of influence paths between professional commitment, work need deprivation, organizational commitment job satisfaction and intention to leave the organization.	1. 1.Organizational and professional commitment in professional organizations is related. 2. In professional organizations, high professional commitment leads to high organizational commitment and both lead to high job satisfaction. 3. For CAs in non-professional settings professional commitment has no effect on job satisfaction.

13	Aranya and Ferris 1984 (OPC)	10% members of CICA, 10% of California Society of Public Accountants.	Analyze the antecedents and outcomes of the organizational professional conflict of accountants working in government, industry and profession.	1. Found that organizational and professional commitment of accountants working in a professional organization was indeed higher than those of accountants employed in non professional settings. 2. The OPC in professional organizations was significantly lower than in non-professional organizations. 3. Correlation between organizational and professional commitment was found to be higher in professional organizations than in non-professional organization.
14	Aranya, Pollock and Amernic (1981)	2590 CAs randomly from all over Canada, in various work settings.	Professional commitment is examined in relation to organizational commitment, professional organizational conflict, satisfaction with income and organizational level.	1. Organizational commitment was the most powerful predictor of professional commitment 2. Highest level of professional commitment shown by partners and sole practitioners and the least by associates. 3. Income and job satisfaction were related. The highest level of satisfaction with income was obtained by partners and sole practitioners and lowest by seniors and semi-seniors. 4. Increasing level of income or the satisfaction with it would contribute positively to professional commitment only for the higher levels of the CA organization.

15	Lachman and Aranya (1986)	Self employed CPAs, CPAs employed in professional organizations, and CPAs employed in non professional organizations	Effects of professional and organizational commitments or of work related attitudes in three different employment settings.	1. Organizational and professional commitment are related under some conditions and unrelated under others, one such condition may be the employment setting. 2. For CPAs in professional organization, commitment to the profession affects organizational commitment directly. Intent to leave may be affected by profession rather than organization related variables. 3. Among CPAs in non-professional settings, intent to leave is positively related to organization related variables and has a weak positive relationship with professional orientation.
16	Meixner and Bline (1989)	State and municipal governmental accountants in five southwestern states	The organizational-professional conflict framework is used to study governmental accountants	Professional commitment positively influences organizational commitment. Findings indicate similarities between governmental accountants and public accountants with respect of traditional job related relationships.
17	Pei and Davis (1989)	45 internal auditors working in departments in 17 companies in Dallas	The purpose of this study is to examine the interrelationships among three variables: organizational structure, organizational-professional conflict and role stress.	1. Organizational structure is an important source variable for both organizational professional conflict and role stress. 2. When internal auditors perceived that their department's organizational structure is not in accordance with the IIA standards, their perceptions of department autonomy were low which in turn resulted in high OPC. 3. Organizational structure was found to directly affect role stress, which in turn affects OPC.

18	Meiksins and Watson (1989) The Sociological Quarterly	585 engineers in the Rochester Area	The purpose of this study was to examine the level of autonomy and conflict experienced by engineers and to relate it to job satisfaction	Supports presence of OPC Need for autonomy-very high (81%) Lowest level of autonomy in the area of time and record keeping (46%) Highest level of autonomy to decide how to do the job (71%) Moderate level of autonomy for access to resource (63%) Lower level of autonomy over choice of project (54%) Job satisfaction positively related to choice of project than structural conditions of the organization.
19	Bunderson (2001) Journal of Organizational Behavior	283 full time clinicians (physicians, physician assistants, registered nurses and nurse practitioners	To examine the effect of perceived administrative and professional breach on professional commitment and turnover intention	Perceived administrative breach positively related to turnover intention Perceived professional breach strongly and negatively related to organizational commitment and job satisfaction and positively related to turnover intention.
20	Lait and Wallace (2002) Industrial Relations	514 human service providers	To examine how professional and bureaucratic conditions at work influence met expectations and job stress	Higher the degree to which work conditions are consistent with professional ideals, greater the 'met expectation level'. Met expectations has a strong negative influence on job stress Higher degree of bureaucracy leads to moderate rise in job stress.

Table 2-2: Example of Studies focusing on Proletarianization Thesis

	Study	Data	Purpose	Results
1	Sorensen (1965)	6 geographically dispersed branch offices of four national public accounting firms	Assess the impact of professional and bureaucratic orientation on job satisfaction and job migration.	1. Partners and managers incorporate a high bureaucratic orientation. 2. The junior and senior associates are characterized by high professional commitment. 3. Bureaucratic orientation is a greater determinant of the level of job satisfaction.
2	Rinehart (1971)	Studies the social networks of blue collar workers and compares them to that of lowest professional employee	To examine whether proletarinization thesis holds	Found distinctive difference between the network of relations of the two groups. Suggests threat of proletarianization of professions is exaggerated.
3	Sorensen and Sorensen 1974	Branch offices of four national public accounting firms	Study the conflicts of professionals (CPAs) in a bureaucratic organization	1. There is an increase in bureaucratic orientation and decrease in professional orientation from lower to higher positions. 2. A CPA with high professional and high bureaucratic orientation will feel greater conflict than the ones with lower orientations.
4	Fox and Wince (1976)	Survey of participation of teachers in political action	To examine whether the teaching profession has undergone proletarianization	Disagrees with the proletarianization thesis suggesting that the rate of participation of teachers in political action groups has remained unchanged despite changes in demography and occupational diversity of the profession.

5	Larson (1980) Theory and Society	Income data on medical professionals, engineers, architects and teachers	To examine the evolving labor process	Three major tendencies observed in all professions: Reduction in stable wages over time causes movement of even specialized professionals to bureaucratic set ups (i.e architects moving to construction firms; PhDs and engineers moving to corporations) Tendency to increase or rigidify the division of professions-with influx of professionals in bureaucratic set ups, there are clearer demarcations of skill and status. Increasing routinization of high level tasks
6	Schutt (1982)	Survey of employees of a public assistance agency	The likelihood of political action by aspiring professions	Finds that aspiring professions would support the rhetoric of political action but not participate in order to signal status.
7	Derber (1983)	Secondary data (dentists)	Examining the kind of proletarianization professionals undergo	Professionals undergo a different process of proletarianization compared to other professional groups. For professionals, proletarianization is indicated by ideological desensitization, ideological cooptation which turns them into professional technicians.
8	Derber 1983 (b)	Employment data on physicians	The process through which proletarianization takes place	Examines proprietary sponsorship relations to suggest that proletarianization for physicians happens through ideological control, bureaucratic control, productivity control and technical control.

9	Whalley (1984)	The distribution of engineers across different organizational settings	Examining proletarianization thesis	Suggests that: Engineers are not undergoing proletarianization. Proletarianization should be studied keeping the labor market condition in mind which would give a better idea of which professions are more likely to resist it.
10	Form (1987)	Official employment and income data	Studies the degree and nature of proletarianization	Suggests that proleterianization is happening across all occupations, despite increasing job complexity and technical intensity. For the professions, the main indicators are reduced autonomy, limited discretion, and increasing stratification.
11	Hagan Huxter and Parker (1988)	Survey of lawyers in the Toronto area	Emergence of the proletariat class within lawyers	Suggests that the young associates in the corporate and commercial departments of large law firms are the new 'proleteriats'. Their high salaries and promising prospects facilitate their domination and limited autonomy with very little chance of rebellion
12	DiPrete (1988)	Case study of professional workers in a government organization	To examine proletarinization thesis	Suggests that functional hierarchies within professions a better indicator of whether proletarianization will happen.
13	Ritzer and Walzak (1988)	Number of physicians working in large bureaucratic organizations	To examine the proletarianization thesis	Changing government policies, changing nature of medical delivery systems and changes within the medical delivery systems driving the proletarinization of physicians, indicated by increased use of technology, increased focus on output, and concern about efficiency and cost accountability.

14	Chua and Clegg (1990)	History of the nursing profession	The attempt in the profession to move away from a proletarian base to a professional base	Difficult for professions to achieve closure if the initial base was socially diffused.
15	Glazer (1991)	Examining the job segmentation within nursing	To examine ways the profession tries to prevent deskilling	Increasing functional differentiation within the profession helped in preventing deskilling but reinforced race and class segmentation.
16	Meiksins and Smith (1993)	Union membership of engineers in Britain and the United States	Examining proletarianization tendencies in different countries	Initial status of the profession was a good predictor of the extent of proletarianization that would happen. In Britain, engineers did not have a high status and were gradually drawn into union membership. In the US, the engineering profession has a relatively higher status and unionization is resisted by the profession.
18	Wright and Jacob (1994)	No of women computer software programmers from 1982-1989	Examining the proletarianization of a male dominated profession	Do not find support for the proletarianization thesis. Find that male programmers are paid higher than comparable women programmers
19	Gallie (1996)	Income and job tenure data (1986-94)	Proletarianization of professions	Finds income gap reducing between professionals and non professionals. Technology and deskilling phenomenon common across the two groups Increased resemblance between Professional and non professional job tenure because of the loss of job security for both groups.

20	Sandefour (2001)	Survey of large law firms in Chicago	The distribution of prestige within the profession	Suggests that functional hierarchies within professions do not solely determine proletarianization threat, a stronger explanation is client relationships. Higher status client base limits the threat of proletarianization.

Table 2-3: Example of Studies Focusing on Adaptation Thesis

No	Study	Data	Purpose	Results
1	La Porte (1965)	Scientists and all managerial personnel of a research division in a major aerospace organization.	Examine the source of strain that might be expected between scientists and managers and some mechanisms that appear to reduce the development of these sources of strain.	1. Managers and scientists differed significantly in the type of career goals, primary research interests and identification with the organization's goals. 2. Administrative procedures of control and coordination were another significant source of strain. 3. Neither organizational structure, authority relations nor rewards were the foci for disagreement or strain. 3. Separation of major functional roles within the organization and mechanisms neutralizing restraining effects of external demands helped reduce strain.
2	Vollmer (1966)	Research scientists in research organizations	What are the various forms that research entrepreneurship may take among scientists? How does it vary in different organizational context? The university, independent research centers, aerospace laboratories, atomic equipment divisions and government research lab.	1. Research entrepreneurship is an important adaptation mechanism that insulates research scientists from the kind of anti-professionalizing pressures existing in some organizational contexts. 2. Individual entrepreneurial activity can be expected to be associated with increased professional productivity in those organizational contexts that are less bureaucratized and that place more emphasis on entrepreneurship as an organizational requirement.

3	Derber and Schwartz (1991)	Large study of scientists, lawyers, doctors and engineers employed in corporations, universities, government bureaucracies, law firms and medical clinics	Argue for the emergence of new relations of production based on professional as well as capitalist power	1. Central concept- logofirms similar to autonomous professional organizations. 2. Professionals have managed to create a logofirm like environment within departments in large corporations. 3. Professionals continue to surrender control, yet they are gaining grounds over issues of how they work. 4. The internal logofirm has become a secure institutional defense against industrial proletarianization. 5. Such melding of apparently contradictory identities may not be stable over the long run
4	Tolbert and Stern (1991)	Sample of approximately 200 law firms in the United States	Examining the determinants of the formal governance structures in two types of decisions-compensation and promotion	1. In large law firms, increased size brings increased formalization but collegial structures coexist with formalized structures. 2. Promotion decisions are still based on collegial structures and follow the norm of peer evaluation. 3. Compensation structures on the other hand evaluate not only the adequacy of the professional's work but also the individual's relative financial worth to the firm.
5	Abernathy and Stoelwinder (1995)	100 physicians and nurse units.	Exploring the interaction between professional orientation and an organization's control environment. Independent variables-professional orientation and control environment. Dependent variable-role conflict, sub unit performance and job satisfaction.	1. The conflict between professional and bureaucratic norms is reduced when professionals with high professional orientation avoid control environments where output controls dominate. 2. Creating an environment, which reduces role conflict, has significant and positive effects on the individual's job satisfaction and overall subunit performance.

6	Wallace (1995)	Compared lawyers working in law firms. Lawyers in government and lawyers in departments on private corporations.	Compared structures of different organizational settings to understand professional and organizational commitment	1. For structural differentiation- found similar levels of autonomy, similar amounts of fairness in the distribution of rewards in all settings. 2. There was more participation in decisions and more task variety in non professional organizations. 3. Professional organizations had less formalization, more promotional opportunities. 4. Commitment difference- those in professional organizations show statistically higher levels of organizational and professional commitment than those working in non-professional organizations. 5. Two variables important in enhancing commitment to the organization- the legitimacy of the criteria used in distributing rewards and autonomy in workplace. This variable is more important for professionals working in non-professional organizations.
7	Bacharach, Bamberger and Conley (1991)	Electronics company specializing in military avionics	Analyze the tension between strategies preferred by professionals and those by administrators.	1. Introduce the metaphor of a see-saw, highlighting 'negotiated order' – organizations are vulnerable to environmental influences. 2. Relative negotiating power of professionals and administrators will vary over time.

8	Kitchener, Kirkpatrick and Whipp (2000)	12 Social Services Departments in England and Wales.	The paper takes the supervision of professional work as the principal subject of study.	1. The public sector there is an attempt at increased bureaucratization of professional work, unlike the trend in private organization towards increased decentralization, flexibility and empowerment. 2. In the public sector, the overall thrust of change has been to establish a more formalized arrangement for monitoring practice. 3. The shift towards a bureaucratic model of control has been far less dramatic and more contested than predicted in the literature.
9	McAuley, Duberley and Cohen (2000)	Focuses on research scientists who work in the public sector.	How professionals make sense of managerialism and deal with it	Find that professionals display a lively and critical understanding of the issues involved with management and at times adopt and absorb new approaches in order to progress their professional work adding to the understanding of ways in which professionals locate management into their understanding of their world.

Chapter 3
Methods

Overview

Chapters 1 and 2 provided an overview of the literature addressing professional behavior and professionals in different organizational settings and professional-client relationships, culminating into the first of the two central research questions in this thesis. This chapter has two objectives: first, it provides an overview of the Enron failure, the specific aspects associated with it, and the justification for using this particular context to address professional behavior. Second, the chapter provides a description of the methods used in the first empirical piece, including the sources of data and the analytic process.

Research Design

Examining the impact of different organizational settings and professional-client relationships on professional behavior generates a number of issues. Foremost, the subject of professional behavior is complex. It involves a multitude of actors and potential causal influences. It also involves a significant contextual component, which warns against easy generalization. In addition, professional behavior (especially misbehavior) is a distinctive phenomenon which represents a significant disruption from taken-for-granted patterns of behavior. Finally, although extant literature offers insight about professional behavior gleaned primarily from quantitative studies, to understand professional behavior that was unanticipated and unique and grounded within a specific social setting, a qualitative case study is warranted.

Why a case study? Case studies are surrounded by complex methodological issues. Some such as Stake (1994) suggest that case study is not a methodological choice but a choice of object to be studied. That is, once a researcher decides to analyze any bounded social system he/she is conducting a case study. Advocates of this view also support a distinctly constructivist epistemology and state that case research is fundamentally reflective and interpretive (Schon, 1985). Others, led by Yin (1984) argue that case study is both the object

of analysis and a distinct method of conducting social research. In this context case research is an essentially positivist analysis and seeks to measure causal relationships between social processes and outcomes through the application of explicitly developed instruments, protocols and related research instruments (Eisenhardt, 1989).

The third characterization is that case studies represent a frame within which social research is to be conducted (Stoeker, 1991). In this context case studies are represented as a framework of time, structure and geography within which data collection can occur. Within such boundaries, social researchers may adopt variety of specific methods to obtain the required information, in this sense a case study is less a method than it is a design structure that houses other methods. In spite of these underlying differences in characterization, the three approaches to case studies share a number of commonalities that reinforce a case method's appropriateness for this research context. These are elaborated below:

Uniqueness: Stake's (1994) observation that choosing to perform a case study is more a choice of object is in large part due to the recognition that case studies are often dictated by the empirical phenomena to be studied. When a researcher decides to study a rare and unusual event, the choice often excludes other research methodologies, such as surveys or experiments, where the intent is to isolate common characteristics of the phenomena and make comparative analyses. Similarly a researcher cannot isolate common characteristics of a phenomenon that has not happened before and is unlikely to be recreated in the same way in a different time and place. The rarity and uniqueness of the event, therefore, dictates the choice of a case study as the appropriate methodology.

The Enron failure and the subsequent indictment of Arthur Andersen affected not only those within these organizations, but more importantly, raised questions about issues of professional responsibility and obligation for a range of other professions. To illustrate, as a direct consequence of Enron's failure and Congressional hearings that accompanied it, the Association of Security Analysts, a professional association, came up with a new code of ethics that was geared towards reducing conflict of interest. Similarly, the Association for Credit Rating Agencies took the initiative to modify their requirements for credit scales mandating a uniform scale for all organizations. Apart from the initiatives taken by the

various professional associations, government too was quick to pass regulation with the intent to ensure the non-occurrence of such events. The Sarbanes-Oxley act was new and path breaking in that it advocated state regulation of an old and established profession. The case study therefore offers a unique opportunity to examine the arena that was the inception for these changes.

Research questions: The type of the research questions set out in this dissertation also justifies using a case study. My interest is in examining the influence of organizational settings and professional-client relationships. An important aspect of this question is to understand not only the impact of the formal aspects of the organization on the individual but also the manner in which individuals are able to negotiate tensions using these formal processes and procedures and interorganizational relationships. A qualitative case study is apt for data that create and illustrate the organization through professional accounts, unlike experiments where the issue is divorced from its context.

The Case: Failure of Enron

The primary focus of this dissertation is to examine the variables influencing professional behavior such as different organizational settings and client relationships. These are studied through the accounts of professionals in Enron, and professionals in Professional Service Firms that Enron associated with; therefore it is important to provide a background to the event.

Enron Corporation was an American energy company based in Houston, Texas, United States. Prior to its bankruptcy in late 2001, Enron employed around 21,000 people and was one of the world's leading electricity, natural gas, pulp and paper, and communications companies, with claimed revenues of $101 billion in 2000. Fortune named Enron 'America's Most Innovative Company' for six consecutive years. It achieved infamy at the end of 2001, when it was revealed that its reported financial condition was sustained mostly by institutionalized, systematic, and creatively planned accounting fraud. Its European operations filed for bankruptcy on November 30, 2001, and it sought Chapter 11 protection in the U.S. two days later on December 2. At the time, it was the biggest bankruptcy in U.S.

history, and it cost 4,000 employees their jobs. In addition, the scandal caused the dissolution of the Arthur Andersen accounting firm.

It was later discovered that many of Enron's recorded assets and profits were inflated, or even wholly fraudulent and nonexistent. This was accomplished by putting debts and losses into entities formed 'offshore' that were not consolidated with (included in) the company's financial statements and by the use of other sophisticated and arcane financial transactions between Enron and related companies formed to take unprofitable entities off the company's books. As the scandal was revealed in 2001, Enron shares dropped from over US$90.00 to US$0.30. As Enron had been considered a blue chip stock, this was an unprecedented and disastrous event in the financial world. Enron's plunge occurred after it was revealed that much of its profits and revenue were the result of deals with special purpose entities (limited partnerships which it controlled). The result was that many of Enron's debts and the losses that it suffered were not reported in its financial statements

Congressional Hearings into the Enron failure revealed that a group of employees had been expressing concerns regarding the accounting procedures and structuring of the special purposes entities as early as 1998. These included some in-house accountants and in-house attorneys as well as senior management rank personnel (Sherron Watkins and Jeff McMahon) both of whom were also qualified accountants. Jeff McMahon, Enron's treasurer asked for a transfer after conveying his discomfort with the financial structures. Sherron Watkins met with then CEO, the late Ken Lay, on August 2001 and handed him a seven page memo detailing her concerns regarding Enron's accounting process and the special purpose entities. She especially highlighted the roles of the external counsel to Enron, Vinson & Elkins, LLP, one of the largest and most respected law firms in the country; and Arthur Andersen, LLP, one of the Big Five accounting firms, as being complicit with the dubious deals. Her concerns were backed up by Jeff McMahon and Jordan Mintz (Attorney and Assistant General Counsel, Enron) and led to an all-employee meeting where more employees conveyed their concerns to the top management. To address the problems, the top management asked Vinson & Elkins to investigate the concerns highlighted by Ms Watkins and others. In October 2001, the law firm reported that apart from some 'bad cosmetics' and instances of 'aggressive and creative accounting', they found no problem with

the SPEs. With regards to the accounting, Vinson & Elkins lawyers conveyed the concerns to Arthur Andersen, who in turn confirmed that they were comfortable with the accounting.

Late in October 2002, SEC opened a formal inquiry into Enron, which also started a devastating trail of events at Arthur Andersen. By the time Andersen received a notice from the SEC in mid-November, a large number of Enron related audit documents were destroyed. Joseph Berardino, the CEO of Arthur Andersen, placed three senior partners associated with the Enron audit on leave and fired David Duncan, the partner in charge of the Enron audit. These actions were seen more as publicity stunts than substantive and subsequently Arthur Andersen, one of the oldest and most prestigious accounting firms in the world, was indicted.

The trial of Arthur Andersen on charges of obstruction of justice related to Enron also helped to expose its accounting fraud at WorldCom. The subsequent bankruptcy of that telecommunications firm quickly set off a wave of other accounting scandals. On June 15, 2002, Arthur Andersen (LLP), Enron's auditor, was convicted of obstruction of justice for shredding documents related to its audit of Enron. Since the U.S. Securities and Exchange Commission does not allow convicted felons to audit public companies, the firm agreed to surrender its licenses and its right to practice before the SEC on August 31. The firm lost nearly all of its clients when it was indicted, and there are over 100 civil suits pending against the firm related to its audits of Enron and other companies. It began winding down its American operations after the indictment. From a high of 28,000 employees in the U.S. and 85,000 worldwide, the firm is now down to around 200 based primarily in Chicago. On May 31, 2005, the Supreme Court of the United States unanimously overturned Andersen's conviction due to flaws in the jury instructions. Despite this ruling, it is highly unlikely Andersen will ever return as a viable business.

Along with Arthur Andersen, there were banks and law firms that were implicated in the Enron affair. The official complaint stated that the Enron fraud perpetrated by the Houston-based energy giant and its auditors succeeded because of the active complicity of several prominent banks and law firms. Nine financial institutions: J. P. Morgan Chase; Citigroup; Merrill Lynch; Credit Suisse First Boston; Canadian Imperial Bank of Commerce (CIBC);

Bank America; Barclays Bank; Deutsche Bank; and Lehman Brothers were named as key players in a series of fraudulent transactions that ultimately cost shareholders more than $25 billion. At the same time, a number of top bank executives profited personally from the schemes. Two law firms were also added to the list of Enron defendants because of their significant and essential involvement in the fraud - Enron's Houston-based corporate counsel Vinson & Elkins, as well as Chicago-based Kirkland & Ellis, which Enron used to represent a number of so-called 'special purpose entities'.

Enron's collapse also led to the creation of the U.S. Sarbanes-Oxley Act, signed into law on July 30, 2002. It is considered the most significant change to federal securities laws since FDR's New Deal in the 1930s. Other countries have also adopted new corporate governance legislations. This law provides stronger penalties for fraud and, among other things, requires public companies to avoid making loans to management, to report more information to the public, to maintain stronger independence from their auditors, and most controversially, to report on and have audited, their internal financial control procedures.

The study examines the Enron-Andersen affair to examine the extent to which organizational forms and models of professionalism help us understand professional behavior. This forms an interesting research avenue for several reasons. First; the Enron affair involves professional behavior in at least two organizational forms - professional service firms (i.e. Arthur Andersen and Vinson & Elkins) and a corporate bureaucracy (Enron). Second, Enron's failure, though large and surprising, is not an exception. It is a part of a series of corporate failure that includes Waste Management, Parmalat, WorldCom and others. Each of these failures deeply implicated the accounting profession and directed considerable attention to other PSFs associated with the failed organization. Subsequently KPMG, Deloitte and Touche, Merrill Lynch, and Citigroup have been examined for questionable practices. Table 3.1 provides a list of the major corporate scandals associated with the largest accounting firms that have been under investigation for unprofessional behavior. Thus, focusing on the Enron-Andersen affair helps not only shed light on a phenomenon that is receiving increasing attention but also directs much needed attention to the significance of understanding the contextual factors in such scandals (Cooper, Everett and Neu, 2005). Enron's failure is also an exceptional case as it led to the indictment and fall

of Arthur Andersen, one of the largest accounting firms in the world. The result of this indictment and investigations into other accounting firms led to the passing of the Sarbanes-Oxley Act. Sarbanes-Oxley has managed to change the accounting profession by limiting the range and scope of services that audit firms can provide, by increasing regulatory oversight of the profession and, finally, by making client firms liable in the case of audit frauds.

Table 3-1: Accounting firm and their investigated clients

Accounting Firm	Client investigated
Deloitte & Touche	Adelphia, AES, Duke Energy, El Paso, Merrill Lynch, Reliant Energy, Rite Aid, Parmalat
Ernst & Young	AOL Time Warner, Dollar General, PNC Bank, Cendant, tax shelter investigations
KPMG	Citigroup, Computer Associates, General Electric, ImClone, Peregrine, Xerox , tax shelter investigation
PricewaterhouseCoopers	Bristol Myers, HPL, JP Morgan Chase, Kmart, Lucent, MicroStrategy, Network Associates, NKFS, Tyco

Data

The study was carried out using transcripts of publicly available Congressional hearings related to Enron. Congressional hearings are important for two reasons: first, as sources of data; and second, as sites for examining policy outcomes. They are unique because of their ability to assemble (by subpoena, if necessary) statements from a wide variety of people knowledgeable about the organization (Wicks, 2001). Congressional hearings are an extremely structured setting and it is expected that people who testify will strive to present accounts of themselves that show them in a positive light. At the same time, these hearings have access to material artifacts such as official policies, internal memos, e-mails and other forms of personal communication, which may either corroborate or contradict the accounts being offered. Table 3.7 provides a list of all the Congressional Hearings that were used in the study.

Enron related Congressional hearings are unique because they brought together people from different professions who provided testimonies not only about the organization but also

about issues such as their perception of professionalism and accountability. The availability of a wide variety of actors makes it possible to get rich and varied descriptions of the internal workings of the focal organizations (Gephart, 1993). The presence of these broad themes is important because the central aim of this paper is not to understand what went wrong at Enron but to examine how professionals in different organizations are able to negotiate, resolve and reconcile terms and content of their work. In order to do so, focusing on how professionals articulate issues pertaining to professionalism, their employing organization, their clients and, their sense of accountability becomes very important.

Congressional scholars acknowledge the importance of hearings calling them a 'fact finding agency' (Huitt, 1954) or a 'safety valve with cathartic effects' (Davidson & Oleszek, 1985). These hearings occur frequently and have an important effect on legislative outcomes (Talbert, Jones & Baumgartner, 1995). However, hearings also present multiple opportunities for strategic behavior by both committee members and those testifying. The committee may be able to control the hearing by determining who may testify, for how long and in what order. Those who testify may withhold crucial information and even intentionally mislead both the committee and the Congress as a whole. These concerns are mitigated by the liberal use of experts who are willing to testify (as in the case of Enron). The testimonies of experts enable the Congressional committee to validate or deem implausible certain accounts presented by witnesses (Deiermeir & Feddersen, 2000).

Scholars hold differing opinions as to what constitutes good qualitative research (Denzin 1997; Gephart, 2004) depending on the ontological and epistemological stance in which they ground themselves. Validity has long been a key issue in debates over the legitimacy of qualitative research. But defining types of validity in terms of procedures, an approach generally labeled instrumentalist or positivist is not the only approach available. Hammersley (1992) suggests that validity is not an inherent property of a particular method, but pertains to the data, accounts and conclusions reached by using that method in a particular context for a particular purpose. In that sense using an archival source of data such as hearing transcripts has various advantages and limitations. First, Congressional hearings such as the ones related to Enron are organized to make sense of the causes and consequences of certain events. Here, people knowledgeable about the event produce native accounts in the

form of testimonies. This gives a researcher the opportunity to examine differences and similarities in the narratives of focal actors. Thus hearings offer the opportunity to investigate how members interpret events and assign responsibility. Second, hearings have access to structural aspects of involved organizations, such as policies and procedures that are publicly not visible. They also use other material artifacts such as minutes of meetings, personal communications and memos as evidence. The presence of these artifacts may complement or contrast the accounts being presented by the focal actors. Third, hearings involve people with varying degree of technical knowledge. This leads to a wide variety of questions that are geared towards understanding, at a more general level, the complexity of the event being studied. For example, in the Congressional hearings involving Arthur Andersen, questions revolved around the accounting procedures used by Arthur Andersen and the destruction of Enron related documents. To understand the technicalities of accounting, many questions focused on issues of professional education and training, code of ethics, rules governing the profession and organizational relationships. This allows a researcher the opportunity to go beyond the focal event and examine in more detail, aspects that influence professional development and behavior. Finally, hearing transcripts of events like Enron and the failure of Arthur Andersen provide insight into the way in which critical but infrequent problems are handled (Gephart, 1993).

However, there are also limitations to using archival data for qualitative analysis. There are at least three main issues which researchers face when dealing with archival data. First, the researcher must make a decision about the degree to which the data is amenable to analysis. For example, data where responses are limited to only a few issues or are short and mostly in monosyllables (which are a possibility in hearings) has limited analytic possibilities. This is not much of a concern in the proposed study. Though the Congressional hearings are structured settings, the questions asked are frequently open ended and involve ample discussion. Further, as these hearings were not geared towards 'judging' but more towards understanding the failure of Enron, most focal actors were forthcoming in offering accounts that could make them look credible.

Another potential concern is the extent to which the archival dataset provides adequate material for a researcher to explore their topic of interest (Hinds, Vogel & Clarke-Steffen,

1997). It may happen that an issue that emerges in one set of transcripts is not addressed in most others. Researchers conducting an analysis of archival data might be constrained in achieving their study objectives if their phenomenon of interest is not consistently present in the entire data set. This could happen either because their phenomenon of interest occurred too infrequently or because the data was not adequately solicited in the time of data generation. In the proposed study, my absence from the setting and lack of access to the focal actors limits my ability to ask more questions that explore professional work issues: tensions, negotiation of work and professional concerns and client relations. However, this limitation can be overcome to some extent by supplementing data using other sources, such as media reports and insider accounts. Studies in the sociology of professions that have examined professional work and related issues also help in informing the study. In order to supplement my data, I made use of insider accounts of Sherron Watkins (Swartz & Watkins, 2003) who was working in Enron, and some Andersen members (Toffler, 2003; Squires, 2003). I read these accounts knowing that they may be offering a biased version of the event. The Congressional hearings that formed the basis of my studies were covered extensively by the popular media and many descriptive accounts are present in newspapers and popular journals. The additional material provided more context to the secondary data. Drawing data from a variety of sources, from hearings, newspapers, popular journals, permits a form of convergent validity (Campbell & Fiske, 1959; Leonard & Barton, 1990). I also consulted publicly available documentation and data that includes analyses by outsiders of similar data. Such secondary source data formed a significant part of my data set. Because the issue of professional responsibility stimulated broad interest in the business press and the media, there were various commentaries on this significant event by business, political and media analysts. This gave me an opportunity to assess the degree to which my preliminary observations corresponded or deviated from those observers.

Newspaper reports from reputable media sources such as *Wall Street Journal*, *Washington Post*, *New York Times* and *Financial Post* were used to supplement the Congressional hearing data. The media reports were utilized in two ways. First, they were used as data supplements. When I found some issues within the Congressional hearings interesting, but could not find enough evidence in the transcripts, I would look for media reports in order to substantiate the issue. As an illustration, some of the professionals in Enron suggested that people within

the organization had been concerned about the accounting decisions and the special purpose entities for a long time. As the transcripts contained only a specific set of testimonies, I searched for media reports that discussed stories of people who voiced their opposition to the top management's activities. The second way in which the media reports were utilized was as a possible indicator of issues related to professional behavior that I did not find convincing. For example, Sherron Watkins' role in the Enron episode was likened to that of a 'hero' (with some justification) by the popular press, but I did not fully concur with this representation and was curious to examine whether the transcripts and accounts of other professionals would tell the same story. A healthy dose of skepticism enabled me to constantly compare what had already been said with what I found in my data.

An issue that is of central concern in qualitative research is *interpretive validity*, which refers to the accounts of meanings that must be based initially on the conceptual framework of the people whose meaning is in question. Social theorists generally agree that any valid account or explanation of a social situation must respect the perspectives of the actors in that situation although it need not be centered on that perspective. One part of ensuring interpretive validity is creating thick descriptions of the event using the actors' own words. In some ways the concept of interpretive validity taps into the notion of clarity and transparency of data analysis (Pettigrew, 1995). The extensive detail and richness of the hearing data along with the supplementary sources can be a boon as well as a bane. While a variety of data sources can provide different versions of the same story, it set before me the temptation of choosing a 'preferred' version. Therefore it was important to ensure that the observations or conclusions were free from bias and that similar observations and conclusions might be made by another researcher. Another way is to increase the plausibility of the inferences by the style of presentation. By using data excerpts to show how preliminary inferences are drawn, I have tried to present them in a way that convinces the reader (Golden-Biddle & Locke, 1993).

It was also important for me to ensure that I remain open to new insights or observations that are outside the theoretical constraints imposed by a particular conceptual framework. During my study, this was best illustrated by the results shown in Chapter 5 which were outside my original theoretical framework. I was initially attentive to identifying the manner

in which centralization and formalization influenced actions and behaviors of professionals. The emergence of an intra-organizational informal network that worked across divisions and groups providing support and credibility to certain kinds of professional accounts surprised me. Objectivity of my observations was also achieved through the opportunity to discuss my research with my advisor and with other interested scholars who provided an important source of feedback that ultimately, helped me enhance the interpretive validity of my observations and conclusions.

It is only through transparent methods of analysis that insights from qualitative research can claim to have *theoretical validity*. Theoretical validity goes beyond concrete descriptions and interpretations and explicitly addresses the theoretical constructions that the researcher brings to, or develops during the study. Theoretical validity thus refers to an account's validity as a theory of some phenomena. Any theory has two components: the concepts or the categories that the theory employs, and the relationships that are thought to exist among these concepts. Corresponding to these two aspects of a theory are two aspects of theoretical validity: the validity of the concepts themselves as they are applied to the phenomena, and the validity of the postulated relationships among these concepts. Theoretical validity is akin to what Sandberg (2005) terms as communicative validity. One way of establishing communicative validity is to discuss the findings with other researchers and professionals in the practice being investigated. By discussing with different communities of interpreters knowledge claims can be refined or challenged as limited. As a researcher, I intend to actively communicate with others in the same field about the plausibility and relevance of the findings of my empirical studies. To do this the data must be integrally linked to the formulated theory. Specifically it requires the researcher to move between theory and data-offering the theoretical analysis augmented with excerpts of data. The use of data tables helps show how data from multiple sources contributes to theory (Golden-Biddle & Locke, 1993).

In short, my endeavor is to ensure that readers are convinced about the logic and transparency of analysis that forms the basis for the insights within the empirical study that follows this chapter

Data Sample

The data consists of publicly available Congressional hearing transcripts. Congressional hearings into the Enron–Andersen affair were held from January 2002 - March 2002. Hearings included testimonies of Enron's senior management, in-house counsel and in-house accountants, Enron's auditors (Arthur Andersen), and external counsel (Vinson and Elkins). In addition, credit rating agencies, financial analysts and investment banks associated with Enron gave evidence. Cumulatively, my data includes about seventeen hundred pages of transcripts recording the testimonies of twenty- four people. In addition we make use of the insider accounts (Swartz & Watkins, 2002; Toffler, 2003; Smith, Squires, McDougall & Yeack, 2003). Insider accounts may offer biased versions of events, therefore I compared them to reports in the Wall Street Journal, the New York Times, the Washington Post and the Financial Times and our transcripts. This process kept me alert to variations, discrepancies and similarities in professionals' accounts.

The table below illustrates the total number of pages, the number of witnesses and the time taken per hearing.

Table 3-2: Summary of Data

Total number of pages of transcripts	1700 pages (not including the appendices which have organizational policies, memos, newspaper articles, emails and personal communication that was offered as evidence.
Total number of witnesses	49 (these include senior partners from the law and audit firms, associated with Enron; top management and in-house accountants and attorneys from Enron; regulators from the SEC and senior management from investment banks and credit rating agencies.)
Time period of the hearings in focus	From Dec 2001-March 2002
Time taken per hearing	Each hearing ranges from a minimum of three hours to a maximum of six hours.

Analytical procedures

The texts were analyzed with an integrated combination of methods: sampling based on theoretical concepts and computer facilitated qualitative data analysis. Sampling on the basis of theory is a way to develop and elaborate a theoretically meaningful subset or sample of

textual data for detailed analysis. Computer facilitated operations include index generation and key word lists, enabling development of theoretical samples. These operations involve disassembling texts and extracting key passages that reveal meaningful topics.

I took one preliminary step before starting with the data analysis. I identified the key personnel who were asked to testify at the Congressional hearings or were given extensive media attention. This was done for two reasons: first, identifying these individuals signaled their importance in the Enron-Andersen affair suggesting that their testimonies would help in unraveling events. Second, for the sake of manageability, it was important for my study to focus on key accounts, because they offered the most amount of detailed information. For the first empirical study (Chapter 5) I identified the key personnel from the focal organizational forms and categorized their responses to all queries about the fall of Enron. These responses are categorized very broadly as accepting responsibility and denying responsibility. This step was taken to get a preliminary picture of the pattern of responses that we may get (Table 3.3).

Table 3-3: Key professionals in the two organizational forms discussing professional responsibility (based on transcripts and media reports)

Organizational form	Organization	Admit responsibility	Deny responsibility
	Enron		
	Richard Causey		X
In-house accountants and counsel	David Woytek	X	
	Jan Avery	X	
	Herb Perry	X	
	Rodney Faldyn	X	
	Ryan Siurek		
	James Derrick		X
	Rob Walls		X
	Rex Rogers		X
	Jeff McMahon	X	
	Jordan Mintz	X	
	Raymond Bowen	X	
	Sherron Watkins	X	
Professional Service Firms	**Arthur Andersen**		
	Joseph F Berardino		X
	David Duncan		Refused to testify
	C.E. Andrews		X
	Michael C Odom		X
	Dorsey L Baskin Jr.		X

	Thomas H Bauer		X
	Nancy Temple		X
	Vinson & Elkins		
	James Derrick		X
	Max Hendrick III		X
	Ron Astin		X
Security Analysts Firms	Gregg Hymowitz, Founding Partner, Entrust Capital	X	
	David W Tice, Portfolio Manager, Prudent Bear Fund	X	
	Marc E Lackritz, President, Securities Industry Association	X	
	Scott C Clelend, Chairman and CEO, PreCursor Group	X	

Stages of Analysis

The data was analyzed in four stages. Each of these four stages is explained in detail below. The first stage involved reading the transcripts of all the Congressional hearings motivated by one central question: *what do these transcripts say about professionals' behavior and their organizational settings?* Reading through the transcripts I realized that issues of professional responsibility were well debated and discussed in the hearings. Nevertheless, in order to ensure that this indeed was the case, I used the qualitative software *Atlas.ti* to run a word frequency count, using synonyms of professionalism and other closely related words. By itself a word frequency count does not amount to much, but it enabled me to utilize every textual segment that included these words and decide whether the segments were pertinent for analysis or not. This was an important step because the hearings were structured in a question and answer format, and many of the words were included in the questions that the Representatives asked those testifying. These segments were set aside, as my central question dealt more with understanding professionals' conception of their responsibilities. I repeated the frequency word count process in order to collect all the pertinent textual segments that dealt with organizational features such as documents, memos, processes and policies. Tables 5A and B provide an illustration of the word count frequency dealing with professionalism and organizational features.

Once all the pertinent textual segments related to professionalism and organizational features were collected, they were separated on the basis of two broad organizational forms: professional service firms and corporate bureaucracy. The textual segments comprising the professional service firms were further divided into specific organizations: accountants in Arthur Andersen; lawyers in Vinson & Elkins; and security analysts from the three different analyst firms. Textual segments in the corporate bureaucratic form included accountants and attorneys working at Enron. Similar sorting was carried out for the textual segments that dealt with organization specific features.

The second stage involved re-reading the textual segments that dealt with professionalism to discern the major themes within the extracts. For example, there were three major issues that were evident in the extracts that dealt with professionalism. These were: *attitude towards work; responsibility;* and *attitude towards clients. Attitude towards work* related to textual segments that included professionals' versions of what they thought constituted professional work. In *responsibility* I focused on extracts that directly or indirectly addressed the extent to which professionals were ready to accept liability regarding work.

Table 3-4A: Key word count for aspects relating to Professional Behavior

Referent Words	Andersen Hearing	Enron/Analyst/ Andersen	Enron Management	Lawyers	Enron/Andersen	Analyst/SEC/Andersen
Behavior						
PROFESSION	6	0	1	1	14	49
PROFESSIONAL	29	7	3	14	5	32
PROFESSIONALISM	0	0	0	1	2	1
PROFESSIONALLY	0	0	0	1	0	0
PROFESSIONALS	3	1	0	2	0	5
PROFESSIONS	0	2	0	0	1	0
PUBLIC	36	21	28	11	49	157
SHAREHOLDER	6	1	6	1	1	17
SHAREHOLDERS	13	55	18	18	16	48
RIGHT	72	129	45	61	21	88
RESPONSIBILITIES	9	16	0	8	8	17
RESPONSIBILITY	39	23	11	33	8	40
RESPONSIBLE	11	20	5	14	7	18
ACCOUNTABILITY	3	0	0	1	0	4
ACCOUNTABLE	4	1	0	0	3	5
ETHIC	0	0	0	0	0	1
ETHICAL	5	3	1	6	1	5
ETHICALLY	0	0	0	1	0	0
ETHICS	5	15	0	9	1	9

Table 3-4B3-5: Key Word Counts for Aspects Relating to Organizational Features

Referent Words	Andersen Hearing	Analyst	Lawyers	Enron
DOCUMENT	126	34	34	30
DOCUMENTATI ON	53	19	2	1
DOCUMENTS	287	45	38	17
RULE	6	46	4	4
RULES	34	74	8	27
MEMO	86	55	24	39
MEMOS	18	23	7	15
REPORT	79	198	91	33
PROCEURE	33	18	5	19
PROCEDURES	16	22	6	25
PROCESS	44	39	17	56
PROCESSES	1	3	3	1

The last issue, *attitude towards clients* tapped into the extent to which professionals' accounts suggested sensitivity to client needs and is illustrated by the examples in Table 3.5A. It is important to note that each of these issues encompassed a small continuum. For example, some professional groups such as lawyers in Vinson and Elkins were very clear about the extent to which they were responsible towards their work. In the case of the accountants at Arthur Andersen, a strong majority of the segments highlighted the limited extent to which they considered accountants were responsible. However, in a few cases some extracts were marginally broader in their understanding of professional responsibility. Security Analysts vacillated most in terms of what they thought constituted responsibility.

Based on the extracts it appears that when it comes to work, accountants in Enron raise issues about the complexity of their work, lawyers about the limited nature of their participation, and security analysts focus on the variables influencing the larger economic environment within which they operate. This theme is echoed by the professional service firms in the case of responsibility when the accountants focus on adhering to GAAP rules, the lawyers focus on the purely legal nature of their advice and the analysts focus on the individual investor's responsibility in following analyst advice. The textual segments of lawyers in Vinson & Elkins tabulated under *attitude towards clients* were very similar to each other. In fact, between all the professional service firms' segments, the lawyers showed the least amount of variability in every issue regarding professionalism. Compared to the professional service firms' accounts, the textual segments of professionals from Enron were different because some of them resembled the segments in the PSFs and a greater number addressed very different issues than those in the PSF organization type. Table 3.5B presents the number of textual extracts that addresses each of the three broad issues: *attitude towards work; responsibility; and attitude towards clients.*

Table 3-5A3-6: Textual segments representing issues related to professionalism

		Attitude towards work	Responsibility	Attitude towards Clients
	Accountants	**Mr. Berardino.** Well, Enron was a very complex company. There is no question that their financial statements and related disclosures are complicated. Many have said that they are difficult to understand. So, again, to the test of do you have the clarity that some are requesting in those financial statements, from that vantage point can an investor understand everything? But very sophisticated investors had those financial statements.	**Mr. Andrews (Partner, Arthur Andersen,LLP)**: Right. So I can't comment on what they would. The company's responsibility and ours is to make sure that those financials are presented and conforming with generally accepted accounting principles, which includes the basic financials and the disclosures as well. And at this point in time those financial statements made by the company have been restated and our opinions have been withdrawn. So that has since changed.	**Rep Stearns**: Is it true that you told our committee staff that some clients in the past had been upset that old or extraneous documents had been unnecessarily maintained and discovered during IRS and SEC inquiries? I mean, our staff indicated that you told them that. Mr. Odom: That's correct.
PSFs	Lawyers	Our work for Enron consisted of a large number of specific projects for which we were selected by the Enron legal department.. Vinson & Elkins, were employed by and directed to interface with Enron's legal department, not Enron's executives. This statement, as well as the testimony that Mr. Astin and I will provide, is based solely upon our individual personal knowledge and best recollection of the events. We cannot purport to know and thus be able to speak to all of the knowledge and information possessed by all lawyers at our firm.	**Mr. Ronald Astin (Lawyer, Partner , Vinson & Elkins):** With regard to the related party transactions, it is important to consider the role of legal counsel. If a transaction is not illegal and has been approved by the appropriate levels of corporation's management, lawyers, whether inside corporate counsel or with an outside firm, may appropriately provide the requisite legal advice and opinions about legal issues relating to the transactions. In doing so, the lawyers are not approving of the business decisions that were made by their clients. Likewise, lawyers are not passing on the accounting	**Mr. Dilg (Partner V&E)**. You have to understand, Mr. Chairman, that in the context that the preliminary review was conducted, Mr. Skilling had just resigned from the company. There was a great deal of speculation in the market and with Enron's counter parties as to the reasons for Mr. Skilling's resignation. We were trying to develop the facts that we could by talking with people inside the company so as not to create lots of speculation and rumors until we knew what we could report to Mr. Derrick. Again, the people that we interviewed indicated that they had seen no business arrangements that were contrary to Enron's best

treatment of the transactions. In conclusion, I want to make it very clear that we are confident that Vinson & Elkins fully met its ethical and professional responsibilities in connection with our representation of Enron

interest coming out of this, or any indication that banks were getting more favorable deals than they should have gotten due to a linkage with LJM. And the person in charge of the banking relationships at that point in time denied there was any linkage.

Analysts

Mr. Glassman. Can I respond to your question, Congressman Bentsen? I think we are telling the American public the wrong thing if the idea they get from this hearing is that the reason that stocks have gone down, or their own accounts have declined, is because of some sort of manipulation that's been going on by analysts.

That's not it at all. The truth is that markets go up and they go down. And in the history of the stock market, one out of every 3 or 4 years, the markets go down. That doesn't mean there's not a lot of pain out there. That's why this hearing is good. But investors have got to understand that markets go up and markets go down and the way to smooth them out is by holding diversified portfolios for the long term.

Mr. Hymnowitz (Security Analysts, Partner EnTrust Capital): In this age of information overload, the individual has the responsibility to perform his or her own due diligence. For decades now, the institutional investor has been ranking equity analysts, and today there are dozens and dozens of free websites, which rank analysts. These resources are doing an excellent job of informing those investors who are willing to invest the time on doing due diligence, and which analysts to follow. But for the individual who merely invests, without doing any of his or her own research on either the issuer or the analyst, does so at one's own peril

Mr. TICE. Yes. If I could respond briefly to Mr. Hymowitz' point, I don't think it is that complicated and you're exactly on target that the analysts should be objective. He should not be looking at what the customers demand for a product or an investment service.

That's the problem. The analyst most often serves as a sales person. He's looking at the customers out there and saying, what can I sell to them; therefore how can I promote this stock so that he will want to buy it, rather than being independent and saying, is this good for the customer. That truly is the problem today.

Corporate Bureaucratic Form	Enron professionals	**Mr. Mintz (Attorney and Asst. General Counsel, Enron):** I wasn't a securities attorney; I didn't deal with PPMs that often, but there were issues here that caught my eye that I thought people should be aware of. **Rep Bass:** And those issues were? **Mr. Mintz:** the sales pitch. It seemed they were trying to sell insider information. **Rep Bass:** You met with Jim derrick, who was Enron's general counsel, several times about your concerns, right? **Mr. Mintz:** I started a process in meeting with Jim after I had completed my due diligence to keep him abreast of what was going on related to LJM.	**Ms Watkins (Accountant, Vice President, Enron):** I think somehow in this country our financial accounting system has morphed into the tax code. And, you know, in the tax accounting, if you follow the codes, whatever results you get, you are justified in using that treatment. In financial accounting, a number of my accounting friends have said if you follow the rules, even if you get squirrelly results, you know, you have a leg to stand on. And I'm surprised that the financial accounting system has morphed into that, because you should still fairly represent your financial condition. That's what's important	**Rep Dingell:** So, am I fair in inferring from this that their statements about the character of these devices as being of benefit to Enron were in error? **Ms Watkins:** Well, a benefit to Enron, if you consider that we were meeting financial statement targets that we had told investor-analysts, but you can't meet those targets falsely. **Rep Dingell:** So, they were- they were essentially represented as being of benefit in the meeting of targets, which could not be met? **Ms Watkins:** Yes, sir

Table 3-5B3-7: Number of Textual Segments Representing Professional Responsibility

Textual extracts regarding work	*Professionals in the Professional Service Firms*			*Professionals in Enron*
	Lawyers	Accountants	Security Analysts	
Attitude towards work	34	87	34	55
Responsibility	17	59	63	78
Attitude towards clients	27	93	44	39

In order to understand the manner in which professionals perceived their employing organization, the textual segments that dealt with organization specific variables such as policies, procedures, memos, hierarchy and culture were divided according to common themes. The four main issues that emerged from the group of textual segments dealing with organization specific variables were: *organizational policies; centralization; organizational systems;* and *others. Organizational policies* included segments that addressed professional's use of specific policies and processes to justify certain actions or inaction in some cases. Focusing on this issue tapped into professionals' perception of the goals of their employing organization's policies and procedures. *Centralization* included segments, which tapped into the sense of autonomy available to professionals in different organizations. The textual segments included the excerpts where professionals alluded to the role their seniors played in influencing certain decisions, and the avenues available for professionals to voice their concerns. *Organizational systems* included textual excerpts where professionals alluded to the compensation policies, training and socialization of their employing organizations. *Others* included extracts where professionals voiced opinions about their perception of what the organizations symbolized, as well as other statements that helped in creating an informal image of an employing organization for the readers.

Table 3.6A provides some illustrative textual segments that tap into professionals' perception of their employing organization. In the case of the professional service firms these textual segments become interesting because they help create an image of the organization through professionals' regard or disregard of the formal structures of their employing organization. In this way, they offer an avenue to examine the assertion of extant literature which suggests

that professionally owned and managed organizations are more nurturing of professional values. Given my familiarity with the research on professionals and organizations, I had expected most professional service firms to be relatively informal, thus I was surprised by the extent to which organizational policies and processes were mentioned by this group of

Table 3-6A3-8: Textual segments representing professionals' perception of organization related features

	Policies and procedures	Centralization	Systems	Others
Accountants	**Ms. Temple:** To the best of my recollection, the firm received a subpoena from the Securities and Exchange Commission the end of the business day on November 8, and a voice-mail was distributed to the audit engagement team notifying them of that the following business day. And once this e-mail was drafted, it was circulated to the engagement team. Now, moving back in timeframe to the previous period that you talked about, the firm does have a written policy that provides guidance. It is self-enforcing, and we trust our partners to exercise their good judgment and to consult with either the legal group or the practice directors, as appropriate.	**Mr. Andrews(Partner, Arthur Andrews, LLP):** With regard to that question, Mr. Chairman, as it is stated in our policy, the responsibility for that rests with the engagement partner, a very seasoned, experienced individual. And we rely on the engagement partner to make that judgment, to make the judgment of what to do, as well as when to seek counsel. Without the knowledge, without our knowledge, without the knowledge of the legal counsel, that meeting was called, that meeting was held, and they proceeded to destroy documents, without consultation, without inquiry as to whether it was proper or improper.	**Mr. Odom.** We were not aware of the meeting that took place on October 23, to the best of my knowledge. So he directed the action. We find that action totally unacceptable. That is why when we began our investigation, which is in process, and we learned of it, we took the action that we have taken to date. But the investigation is in process and not completed. We took the action aggressively, because it is a situation we will not tolerate. It is not the way Andersen personnel are trained to perform, and it is completely unacceptable. So it is totally out of bounds with good judgment in that situation. And we took action as a result of that.	

PSF	Lawyers	**Mr. Astin**: I want to make it very clear that we are confident that Vinson & Elkins fully met its responsibilities in connection with our representation of Enron. We had policies in place to ensure the above and we are pleased to assist in the committee's deliberations and are happy to answer your questions within the constraints of our professional responsibility.	**Rep Stearns:** Mr. Skilling didn't sign these documents and why you, as a former general counsel of Enron didn't get a concern when Skilling didn't sign these? **Mr. Astin (Partner, Vinson & Elkins, LLP)**: Well, Congressman, as we have said, we had almost 150 lawyers in a decentralized department- **Rep. Stearns** You had too many people to enforce the signing of the document? **Mr. Astin**. No, but the responsibility for that was allocated by the board to Enron Global Finance and their attorneys. **Mr. Sefton (Attorney and Asst General Counsel, Enron)**: I'd like to just say that it was never my understanding that the board delegated this job to Enron Global Finance legal. That was never my understanding.	**Letter from the Partner, Vinson& Elkins to General Counsel Enron** … in preliminary discussions with you, it was decided that our initial approach would not involve the second guessing of accounting advice and treatment provided by Arthur Anderson, that there would be no detailed analysis of each and every transaction and there would be no full-scale discovery style inquiry.

Analysts

Mr. Lackritz. Could I address that first, Congressman? I think that these best practices that we've come up with are going to be very effective, and are going to work extremely well. The reason for that is because they've been endorsed not only by the 14 largest firms representing 95 percent of the underwriting business, but all the CEOs of those firms down through the directors of research. In addition, you've got an incredibly powerful and unforgiving enforcer in the marketplace. These practices are designed to help improve the quality of research. To the extent that the quality of research doesn't improve for clients, they go other places. To the extent that competitors see that their competitors may not be following some of these rules, they're going to be quite aggressive.

Already you see a fair amount of competition in the marketplace.

David W Tice. Our interest in testifying is clear. We are worried that the powerful investment banking and trading interests that have suffocated independence within a firm are at work within the industry at large, and can suffocate the independent research views at large.

That's because the firms that have conflicts control well over 90 percent of the market for research commissions, according to our best estimate.

Scott C Cleland: The communication between analyst and issuers is symbiotic. The issuer needs the analyst's coverage to get potential investors interested in buying, and the analyst's life blood is an open communication channel to the issuer. Of course, we have issue of distance, but one can surmise that communication is easier and more open between parties when they are aligned. And really if the firm performs, it helps all of us regardless of which side we are on.

Corporate Bureaucratic Form	Enron Professionals	**Rep Greenwood**: What do your initials signify? Why did you put your initials on that document? **Ms. St. Clair (Attorney, Enron)**: They signify that as the lawyer that was in charge of representing Enron's side in the Chewco transaction, that the document satisfied the legal criteria, that it was okay for the officer to sign from a legal perspective. **Rep Greenwood.** Okay. But you don't know why it was drafted in a separate document. I mean you looked at it and you decided that it was okay for the executive to sign. You had done your legal scrub of it-- **Ms. St Clair.** Right.	**Rep Tauzin**: Now, did you ever have a conversation with him about the precarious financial condition of Enron and its reliance upon these questionable deals to continue to meet the earnings projections? **Ms Watkins**: I had worked with Mr. Buy during the time period where I was managing the JEDI portfolio. I have also had discussions with him-you know, he was a former co-worker and friend. The week leading up to my meeting with Mr. Lay, Mr. Buy was on vacation, and I actually phoned him. I was trying to use him as a sounding board as well. I told him a bit about my concerns, and that I had a meeting scheduled with Mr. Lay. I asked him if I could fax him my materials to get his opinion of my concerns. **Rep Tauzin**: Now, did you tell him that in fact some of the materials had come from his own shop? **Ms Watkins**: No, but I just told him I had some memos that I wanted to fax him, and have him look at.	**Ms Watkins**: On August 21st, I met with [redacted]. McMahon, for roughly an hour-and-a-half. I mean, that is when he told me that he found the conflicts to be-to be something that-you know, too great. He said they're making it all about the money, but it shouldn't always be about getting the highest bonus, he said.	**Ms Watkins**: She encouraged me to meet with Mr. Lay, which I did do. I then subsequently transferred into Ms. Olson's group. I did not have lengthy conversations with her after that about my concerns. When I met with Mr. Lay on the 22nd, I was leaving for a small vacation that Friday, coming back the following Thursday. When I came into the office August 30th, I had messages to immediately go see Ms. Olson. And that is when she told me that Mr. Fastow had wanted to have me fired and wanted to seize my computer. But Ms. Olson basically said, Let me send you to your office with an IT person-here's a new laptop-transfer whatever files you want to on the new one-delete whatever ones you want to on the old one-we'll just

Ms Watkins (Accountant and Vice President Enron): Well, all I can say is-all I can speak to is that it was Enron's very strict policy, when completing transactions and deals, to have deal sheets, deal approval sheets, and there was never a name put on the approval block that was not required. And I don't ever remember an instance where signatures were not obtained for every person listed.That's-that would be my understanding of our very strict procedures, yes.

Rep Tauzin: Were those procedures that Mr. Skilling would have understood?

Ms Watkins: Yes

Rep. Stearns. Did you sign the approval sheets for the LJM2?

Did you sign them?

Mr. Sefton. Yes, I did.

Rep Stearns. Now if you signed them that meant that you were approving the LJM2 partnership, is that correct?

Mr. Sefton. That is not my understanding.

Rep Stearns. So when you sign a document that's the approval sheet, it's your understanding that that does not mean it's an approval sheet?

Mr. Sefton. The approval sheet requires approval by Mr. Buy and Mr. Causey. Those were the two senior executive officers of the company who were required to approve the transactions by the board of directors.

Rep. Stupak. Is it true that Mr. Buy advised you not to stick your neck out by approaching Mr. Skilling with your concerns about LJM?

Mr. Mintz. Well, I got with Mr. Causey, Mr. Buy when I wanted to approach Mr. Skilling about reviewing the documentation and making sure they were executed and finding out whether it was ministerial or not. And I also suggested maybe we should check with Mr. Skilling to make sure he is still comfortable with this arrangement. And, yes, Mr. Causey said, ``I wouldn't stick my neck out. You wouldn't want to ruin your next evaluation, would you?''

Rep Stupak. Mr. Causey said that----

hand him the hardware. She said, "You don't mind doing that, do you?" And I said, "No, I don't."

Mr. McMahon. Yes. I have known Sherron for several years.

Chairman Tauzin. Did you know about her August 14 or 15 memo to Mr. Ken Lay describing what she considered to be problems that might amount to an implosion of the company and a wave of accounting scandals?

Mr. McMahon. She sent me a copy of that one-page letter after she had delivered it to Mr. Lay. And then she came and we spoke about it.

Chairman Tauzin. Did you speak to Mr. Lay about Sherron Watkins and her letter?

Mr. McMahon. I did. When Sherron came by to see me, I encouraged her to

actually take authorship of that letter and see Mr. Lay directly.

Chairman Tauzin. That is to not do it anonymously but to let him know it was she who was writing it. Did you recommend her to Mr. Lay?

Mr. McMahon. I did. I called Mr. Lay and explained to him that although I was unaware of any of the facts in her letter, I did validate that Ms. Watkins was in fact a reputable source and employee and she should be listened to with----

Chairman Tauzin. So you did vouch for her to Mr. Lay?

Mr. McMahon. That is a fair assessment.

professionals. The manner in which professionals in different PSFs described policies, hierarchy and other aspects of their organizations varied a little. For example, the accountants in Arthur Andersen mentioned specific policies within their organizations. The security analysts in turn discussed centralization, policies regarding rewards and compensation, and other informal aspects that were common to all the analyst firms represented in the Congressional hearing. The lawyers most carefully avoided mentioning specific policies or formal arrangements. Even as they discussed organization specific features, they were very careful to qualify it as their 'personal' understanding of a specific feature.

The professionals in the corporate bureaucratic form were much more frequent in their reference to specific organizational policies, alluding to how their actions were constrained or enabled by the system in place and the general culture of the organization. While most of the textual segments exhibited aspects of one or more of the above three issues, I encountered a set that was not easily classified into any of these issues. Surprisingly, this set of segments was present exclusively in the accounts of professionals from Enron and alluded to an intra-organizational network not evident in any of the professional service firms. Table 3.6B shows the number of textual segments present in each of the four issues dealing with organizational specific features.

Table 3-6B3-9: Number of Textual Extracts Focusing on Organization Specific Features

Textual extracts referring to organizational settings	***Professionals in the Professional Service Firms***			***Professionals in Enron***
	Lawyers at Vinson & Elkins	Accountants at Arthur Andersen	Security Analysts	
Organizational policies	21	52	49	75
Centralization	19	31	28	32
Systems (compensation, training and socialization)	20	48	51	46
Others	0	0	0	24

In stage three I went back to the textual extracts now separated by three issues in the case of professionalism (four, in the case of organization specific variables) to reconstruct a narrative that gave an idea of the sense of professionalism from each of the professional service firms and corporate bureaucratic forms. In other words I was interested in creating narratives that addressed the manner in which different groups of professionals in different organizations perceived various issues related to professionalism. These were done for each of the professional organizations and the corporate bureaucratic form. The result of this endeavor led to some surprising observations. First, there was tremendous similarity in the manner in which all the professional groups in professional service firms envisaged professionalism. Their sense of responsibility and attitude towards clients were remarkably similar. Second, the corporate bureaucratic form had two versions of professionalism. One was similar to the version in the professional service firms, and the other was very different. Similarly, a narrative was created for each of the issues that constituted organization specific variables. Again, as in the previous case, all three groups of professionals in professional service firms shared very a similar perception of their employing organizations. However the professionals in the corporate bureaucratic form had differing versions.

In the fourth stage, I compared the summarized narratives representing aspects of professionalism across different organizational types. This led to the identification of higher order categories across which the issues identified in stage three differed. Across the two organizational types, perceptions of professionalism differed by two categories: *task boundedness*, and target of accountability. Task boundedness encompasses both attitude towards work and responsibility. It addresses the extent to which professionals actively and deliberately draw boundaries around task definitions and professional liability issues. Target of accountability includes aspects of a professionals' attitude towards clients and their sense of responsibility. It addresses professionals' perception of who they are ultimately answerable to. Interestingly, comparing task boundedness and target of accountability across the two organizational types led to an observation similar to that of stage three. All professional service firms illustrated the same and single understanding of task boundedness and target of accountability. The corporate bureaucratic form, on the other hand, had two versions of the task boundedness and accountability. One was similar to that of the professional service firms and another was very different. At this point, I went back to the

literature on professionalism to explore insights that would help me examine my inferences better. A piece that guided me in this process was Brint (1996), where he addressed the notion of changing models of professionalism. According to him, the model of professionalism changes over time depending on the environment within which professions operate. Brint (1996) speaks of a traditional model of professionalism (termed as the social trustee model) that has been replaced by a new model of professionalism, which he terms the expertise-based model. The two higher order categories of task boundedness and target of accountability appeared similar to the values underlying these two models of professionalism. In the case of professionals' perception of organizational specific features, issues of hierarchy, organizational policies and procedures, and informal aspects resulted in creating an image of organization that was either high on formalization or was largely informal. In line with the literature on professionals and organizations, the professional service firms in my analysis were predominantly informal, while the corporate bureaucratic form appeared much more formal. This led to a puzzle: if professional service firms were more informal, why were all of them characterized by a single model of professionalism, and why was the corporate bureaucratic form able to accommodate two very different models of professionalism? In order to understand how a certain organizational form was able to accommodate multiple models of professionalism, I revisited stage three to focus on a subset of textual segments where professionals discussed aspects of professionalism along with their perception of their employing organization. This process of iteration between data and theory helped me arrive at the central concept of 'professional space', which is introduced and elaborated in the empirical study.

In summary, the central motivation of this chapter has been to explain the empirical focus and the methods used in this thesis. The next chapter elaborates upon the two professional models, and connects them to organizational forms.

Table 3-73-10: List of Congressional Hearings

	Hearing before the Committee on Governmental Affairs United States Senate.
Hearing 1	
Date	March 20th 2002
Focus	Rating the Raters: Enron and the Credit Rating Agencies

Testimonies of	**a)**	**Ronald M. Barone**	Managing Director, Corporate and Government Ratings Group, Standard and Poor's
	b)	**John C. Diaz**	Managing Director, Moody's Investor Services
	c)	**Ralph G. Pellicchia**	Senior Director, Global Power Group, Fitch Ratings.
	d)	**Hon. Isaac C. Hunt Jr.**	Commissioner, U.S. Securities and Exchange Commission.
	e)	**Jonathan R. Macy**	Professor of Law, Cornell Law School
	e)	**Glenn L. Reynolds**	Chief Executive Officer, CreditSights Inc.
	e)	**Steven L. Schwarcz**	Professor of Law, Duke University School of Law

Hearing 2	Hearing before the Subcommittee on Oversight and Investigations of the Committee on Energy and Commerce, House of Representatives.		
Date	March 14th 2002		
Focus	The Financial Collapse of Enron		
Testimony of	**a)**	**Ronald T. Astin**	Partner, Vilson and Elkins, LLP
	b)	**Joseph C. Dilg**	Managing Partner, Vilson and Elkins, LLP
	c)	**James V. Derrick**	Former General Counsel, Enron Corp.
	d)	**Rex R. Rogers**	Vice President and Associate General Counsel, Enron Global Finance, Enron Corp.
	e)	**Carol L. St.Clair**	Former Assistant General Counsel, ECT Resources Group, Enron Corp.
	e)	**Scott M. Sefton**	Former General Counsel, Enron Global Finance, Enron Corp.

Hearing 3	Hearing before the Subcommittee on Commerce, Trade and Consumer Protection of the Committee on Energy and Commerce. House of Representatives.		
Date	March 4th 2002		
Focus	A Review of FASB action post Enron and WorldCom		
Testimony of	**a)**	**Robert H. Hertz**	Chairman, Financial Accounting Standards Board

Hearing 4	Hearing of the Oversight and Investigations Subcommittee of the House Energy and Commerce Committee on the financial collapse of Enron Corp.		
Date	14th of February 2002		
Focus	Financial collapse of Enron Corp.		
Testimony of	a)	**Sherron S. Watkins**	Vice President, Enron Corp.

Hearing 5	Sub-Committee on oversight and investigations of the committee on energy and commerce, house of representatives, 107th Congress		
Date	7th of February 2002		
Focus	Financial collapse of Enron Corp.		
Testimonies of	a)	**Jeffrey Skilling**	Former President and CEO of Enron Corp.
	b)	**Jeff Mc Mahon**	President and Chief Operating Officer of Enron Corp.
	c)	**Thomas H. Bauer**	Partner, Andersen LLP.
	d)	**Robert Jaedicke**	Member, Enron Board of Directors and Chairman of the Enron Audit and Compliance Committee
	e)	**Jordan H. Mintz**	Vice President and General Counsel for Corporate Development
	f)	**John Olson**	Senior Vice President and Director of Research, Sanders Morris and Harris
	g)	**Herbert S. Winokur, Jr.**	Member, Enron Board of Directors, Chairman of the Finance Committee

Hearing 6	Hearing before the Committee on Energy and Commerce, House of Representatives		
Date	February 6th 2002		
Focus	Lessons learnt from Enron's Collapse: Auditing the Accounting Industry		
Testimonies of	a	**James S. Chanos**	Kynikos Associates Ltd
		Bala G. Dharan	Rice University
		Baruch Lev	New York University
		Bevis Longstreth	Debevoise & Plimpton
		Roger W. Raber	National Association of Corporate Directors
		David L. Sokol	Midamerican Energy Holdings Company
		Roman L. Weil	University of Chicago

Hearing 7	Hearing before the Subcommittee on Capital Markets, Insurance and Government Sponsored Enterprises of the Committee on Financial Services, U.S. House of Representatives.		
Date	February 4th and 5th, 2002		
Focus	Implications to investors and the capital markets		
Testimony of	a)	**Hon. Harvey L. Pitt**	Chairman, U.S. Securities and Exchange Commission
	b)	**William C. Powers**	Chairman of the Special Investigative Committee of the Board of Directors, Enron Corp.
	c)	**Joseph F. Berardino**	Chief Executive Officer, Arthur Andersen LLP

Hearing 8	Hearing of the Subcommittee of Oversight and Investigations of the Committee on Energy and Commerce House of Representatives		
Date	24th of January 2002		
Focus	Destruction of Enron-related documents by Andersen personnel		
Testimonies of	a)	**David Duncan**	Andersen partner, in charge of the Enron account
	b)	**C. E. Andrews**	Senior executive, Andersen LLP.
	c)	**Michael C. Odom**	Audit Partner, Andersen LLP.
	d)	**Dorsey L. Baskin Jr.**	Managing Director, Professional Standards Group, Andersen LLP.
	e)	**Nancy Temple**	Attorney, Andersen LLP.

Hearing 9	Hearing before the Subcommittee on Capital Markets, Insurance and Government Sponsored Enterprises of the Committee on Financial Services U.S. House of Representatives		
Date	June 14th and July 31st, 2001		
Focus	Analyzing the Analysts		
Testimonies of	a)	**Thomas A Bowman**	CFA President and CEO, The Association for Investment Management and Research
	b)	**Scott C. Cleland**	Chairman and CEO The Precursor Group
	c)	**Benjamin M Cole**	Financial Journalist and Author
	d)	**James K. Glassman**	Resident Fellow, American Enterprise Institute.
	e)	**Gregg S. Hymowitz**	Founding Partner Entrust Capital.
Testimonies of	f)	**Marc E. Lackritz**	President, Securities Industry Association
	g)	**Damon A. Silvers**	Associate General Counsel, AFL-CIO
	h)	**Benjamin M Cole**	Financial Journalist and Author
	i)	**David W. Tice**	Portfolio Manager, Prudent Bear Fund

Hearing 10	Joint Hearing before the Subcommittee on Capital Markets, Insurance and Government Sponsored Enterprises and the Subcommittee on Oversight and Investigations of the Committee on Financial Services, U.S. House of Representatives.		
Date	December 12th 2001		
Focus	Implications to investors and the capital markets		
Testimony of	a)	**Charles L. Hill**	Director of Research, Thompson Financial/First Call
	b)	**Richard L. Trumka**	Secretary-Treasurer, AFL-CIO
	c)	**Joseph F. Berardino**	Chief Executive Officer, Arthur Andersen LLP

Chapter 4
Exploring Professional Space

Introduction

The previous chapter discussed the various stages of analysis, the results of which will be elaborated in this chapter. The analysis resulted in two interesting observations: first; different groups of professionals hold differing conceptions of professionalism; and second, organization forms differ in their ability to accommodate certain models of professionalism. These observations are important and interesting for several reasons. Most of the professional service firms associated with Enron and the subsequent corporate failures were criticized for being 'unprofessional', reneging on their responsibility, and for being unethical. Interestingly, the analysis shows that professionals may conceptualize professional responsibility and hence professional conduct in different ways. For example, the Congressional Representatives found a certain set of behaviors that was in consonance with their expectations from professionals and labeled it 'professional behavior'. This set of behaviors included voicing concern over issues of professional decision making that appear to be inappropriate, ensuring that people in the organization who have the resources to mitigate the concerns know about it, taking initiative to examine issues of concern in more detail, and most importantly, privileging the unorganized investor's interest.

The kind of conduct eulogized by the Congressional Representatives, the media, and the public in general conformed to a certain model of professionalism, which Brint (1996) terms the *social trustee* model. However, professionals in the professional service firms also defended their decision-making and behavior, which, according to them conformed to expected standards. Their version of professionalism differed distinctly from the social trustee model and was closer to the model that Brint (1996) terms the *expertise based* model of professionalism. The presence of at least two models of professionalism highlights the need to move beyond the traditional manner of studying professionalism on the basis of autonomy, collegiality, and peer review that characterize studies in the sociology of

professions, and examine more the contextual factors that may influence professionals' attitude towards work and responsibility.

In addition, the observation that all the professional service firms strongly espoused the expertise based model suggests that employing organizations play an important role in influencing professionals' attitude towards work and responsibility. Professional service firms' endorsement of the expertise based model is an interesting result by itself because much of the literature on professionals and organizations suggests that professional organizations are more 'professional friendly' and more nurturing of professional values. A logical expectation would be to assume that what constitutes professionalism for the broader audience, i.e. the social trustee model, will be reflected within organizations that are owned and managed by professionals. Therefore, the absence of instances of the social trustee model and the dominance of the expertise based model of professionalism in all of the professional service firms is surprising and contrary to prevailing theory. More surprising however, is the fact that the social trustee model was found in an organizational form typically seen in the literature as 'professional unfriendly', i.e. the corporate bureaucratic form. But this was not the only difference between the corporate bureaucratic form and the professional service firms. The corporate bureaucratic form was different from the professional service firms in another key way: the corporate bureaucratic form accommodated *both* models of professionalism.

The results suggest that professional behavior indicated by whistle blowing, dissent, and initiative, is more likely to happen in an organizational form that can accommodate multiple models of professionalism. Therefore, the central aim of this chapter is threefold: first, to detail the two models of professionalism; second, to establish that certain organization specific features enable and constrain the accommodation of these models; and finally to propose that professional behavior is enabled by access to different models of professionalism. This will lead to the introduction and elaboration of the central concept of the chapter - *professional space* - the ability of professionals to maneuver organizational and professional concerns.

Multiple models of professionalism

The two models of professionalism, the expertise based model and the social trustee model, differ on the basis of two key attributes: the degree of *task boundedness*, and the *target of accountability*. The expertise based model has a high task bounded approach to professional work, combined with a rule centric view of accountability. Both these characteristics are achieved using three main tactics. First, professionals creatively and consistently draw boundaries around their perceived areas of responsibility. In doing so, they argue for accountability that is limited to the correct completion of individual task. Second, professionals focus on the complexity of professional work, thus playing up the role of rules in managing complexity meaningfully. Finally, professionals subscribing to the expertise based model of professionalism attempt to portray conflict of interest as something normal and usual in the course of professional work. The combination of portraying rules as central to and conflict as a normal aspect of professional work, results in the marginalization of the interests of the individual investor.

In contrast, the core attributes of the social trustee model are low task boundedness, i.e. a holistic view of professional work, combined with an investor centric view of accountability. Professionals espousing the social trustee view of professional work use two main tactics in order to achieve the core characteristics. First, professionals focus on the relationship between different components of work, even though they may be tasks handled by different people. Second, there is a strong insistence on examining the intent and consequence of professional work. By having a view of work which is low on task boundedness and focusing on the ramifications of their output, professionals are able to achieve a sense of accountability that puts the individual investor and his/her interests central.

The differences between the two models of professionalism will be illustrated and discussed in detail below:

Expertise Based Model

(a) High task boundedness. Task boundedness encapsulates the manner in which professionals view their work as well as their responsibility. The analysis suggests that professionals in

professional service firms claimed to have clearly delineated tasks (i.e., high task boundedness), therefore their sense of responsibility was limited to the completion of the task without paying attention to the manner in which it contributed to the larger project. The example below suggests the task boundedness approach.

> **Mr. Dilg:(Partner, Vinson&Elkins)** As far as looking at Chewco, Mr. Kopper did negotiate on behalf of LJM and was reflected as doing so in the LJM approval sheets that were signed off on by the two people that the board had established to make sure that the deals were done on a basis that was favorable to Enron. There was a service agreement that was signed by Mr. Causey on June 30th 1999.
> **Chairman Tauzin:** But Causey and Buy aren't in the office of the Chairman, you know that. They can't give waivers, you know that. You just testified that the office of the Chairman was the only one that could give a waiver, not Causey and Buy, is that right?
> **Mr. Dilg:** That is correct. We did not check on the waiver of the code of ethics issues. There were signatures on the approval sheets from Enron's side.

In the above extract, lawyers from Vinson & Elkins (Enron's external counsel) are asked why as external counsel to Enron they neglected to warn their client against actions that amounted to conflict of interest. The lawyers suggest that they were being correct in designing their professional work around the protocol of the client organization, that their responsibility was limited to expressing their opinion on the deal and not to examine whether there was any conflict of interest. Any work before their involvement had to be done by the client organization. Therefore, in this case despite having information that should have alerted them to potentially problematic issues, the lawyers checked only for the signatures in the approval sheets.

This approach to work, which splits a project into a series of tasks, achieves one central objective: it enables professionals to disassociate the ethical responsibility from their bounded task. Because each professional is assigned a small portion of the entire project, no one has to take responsibility for the consequence of a cumulative project. Thus, if anything were to go wrong, the blame can be passed down from one person to the other. This kind of task boundedness was also exhibited by Enron's in-house attorneys.

> **Rep Green**: Okay. The proxy (on the financial statements) states that, "management believes that the terms of the transactions were reasonable and no less favorable than the terms of similar arrangements with unrelated third parties." Mr. Derrick, Mr. Sefton and Mr. Astin, tell me what basis you had on signing off on the statement, and what was the due diligence that these representations called for?
> **Mr. Derrick (Ex-General Counsel, Enron)**: Congressman, speaking for myself, I didn't have a personal involvement with that. We had in place what we considered to be a large

team of qualified people who would have been looking at that and preparing the proxy statements.
Rep Green: Well, who was in charge?
Mr. Derrick: Well, internally Mr. Rogers was leading our securities effort.
Rep. Green: Mr. Rogers, did you sign off on that statement?
Mr. Rogers (Associate General Counsel, Enron): I was part of the team that was charged to gather the information. I did not do the personal due diligence. I didn't draft the proxy disclosure.
Rep Green: But you signed off on it.
Mr. Rogers: Well, when you say signed off on it, I reviewed it and based on the information that was presented to us, we agreed with it.

Very similar to the lawyers in Vinson & Elkins, this extract highlights more clearly the extent of the limited view of work that some groups of professionals have. Here, professional work appears to be broken into at least three sets of tasks: gathering information and conducting due diligence; drafting the proxy statement; and agreeing with the information that is presented. The attorney who ultimately takes responsibility for the completed task, limits his liability to 'reviewing the information' presented. This notion of a restricted view of decision-making and of work is indicated in the manner in which a partner from Vinson & Elkins framed his testimony.

Mr. Astin (Partner, Vinson & Elkins): Of course, had I been blessed with the gift of clairvoyance, had I been permitted to gaze into the future and foresee the events that would unfold in respect of Andersen, I would have advocated the choosing of another path last August. But that was a gift I was not given. The decisions in which I participated had to be, and were, made in the context as matters then existed.

The Vinson & Elkins partner defended all of his decision-making by highlighting the limited information that influenced his professional choice which he argues should limit the extent of his professional liability.

Thus, there is a strong tendency for professionals working in professional service firms to approach professional work as a series of tasks that need to be executed without being related to each other. In taking responsibility for limited aspects of work and drawing boundaries on the basis of expertise, experience or position, professionals in this organizational form are unable to see the professional work in its entirety and therefore unable to appreciate the consequence of such work for the investors.

(b) Target of accountability: rule centricity.

Target of accountability alludes to professionals' understanding of whom or to what they are ultimately responsible. As professionals focus on carved out tasks and ignore the larger picture of which the professional work may be a part, they are likely to look for targets of accountability that are clearly stated and easily defensible. This is illustrated in the manner in which professionals in the PSFs explain their actions.

> **Mr. Berardino (CEO, Arthur Andersen, LLP):** The company's responsibility and ours is to make sure that those financials are presented and conforming with generally accepted accounting principles, which includes the basic financials and disclosures as well. I would also like to correct the record in one respect, because people keep saying things like we set these things up. Our firm where—the accountants and the accounting advisors' management, in conjunction with their investment bankers, lawyers and others, would present us a transaction and would ask the obvious question, does this pass the rules? And we would give our judgment as to whether it would pass the rules, and at the end of the day those judgments were rendered.

In this extract the CEO of Arthur Andersen is discussing what he views as his firm's responsibility and in doing so, clearly identifies the GAAP rules as its target of accountability. A target of accountability that is a set of written rules is both defensible and seemingly clear. Rules provide a fairly clear distinction between what is permitted and what is not; at the same time they offer the opportunity for interpretation that can be fairly subjective. Another interesting tactic used by professionals in PSFs to play up the importance of rules was to highlight conflict of interest, and failures of the profession as a normal process. This is done for a few reasons. First, in emphasizing conflict of interests as a normal aspect of professional work, the pressure to be morally sensitive is reduced. Second, rules become more central to the profession in order to reconcile seemingly opposing roles. This is suggested in the extract below.

> **James K. Glassman (Security Analyst, American Enterprise Institute)**: Analysts and firms have enormous incentives to do their jobs well. The marketplace always weeds out the bad from the good. Conflicts of interest pervade the securities industry because they pervade life. You Members, yourselves, cope with conflicts all the time. You have allegiances to family, to donors, to party, but you try to surmount them. For stock analysts, their judgments are clear and more easily accessed by the public. An analyst who consistently gives bad advice will be rejected as not useful, either to investors or ultimately to the firm that employs her.

The above extract is interesting because of the manner in which the professional attempts to portray conflicts of interest as a regular aspect of professional work. In doing so, he attempts two things First, when conflicts are normalized, seemingly conflicting roles can be still be seen as being appropriate. Second, in highlighting the conflicts present in professions, the

role of rules becomes more important - they can be the objective mechanisms through which conflicts are resolved and reconciled. The extract below further illustrates this tendency.

> **Mr. Castellano (President AICPA):** We don't believe that there is an inherent conflict in auditors performing non audit services for their clients, that there are safeguards and rules that must be followed within our code of ethics today, and if those rules are followed, the auditor's judgment would not be impaired.

In the above extract, the president of the AICPA suggests that two sets of seemingly opposing sets of responsibilities, that of an auditor (who should ensure that the financial condition of the firm is represented fairly for the individual investor), and that of a consultant (whose main motivation is to ensure that the client organization appears as an attractive investing target to the investors *without taking into account* the investor's interests), can be managed meaningfully if a set of rules are followed. Here, the importance of rules is emphasized despite the inherent difference in the role of an auditor (which demands some distance from and an objective assessment of the firm's finances), and that of a consultant (which entails very close and cooperative involvement with the client organization).

Another tactic of ensuring that rules remain the primary target of accountability is to marginalize any other constituent that claims to be influenced by professional output. In the case of professionals subscribing to the expertise based model, it is the marginalizing of the claim of the individual investor.

> **Mr. Hymnowitz (Security Analyst):** Congressman, let me answer the question...prospectuses that this Government requires companies to file hopefully are meant to be read. And the individual who does not want to spend time and the effort to read the prospectus then should do what millions and millions of Americans do every day, and that is give their hard-earned investments to mutual fund companies to index funds, to brokers, to money managers to hedge funds. Look, I don't know anything about automobiles, so if I go in and I attempt to figure out what car to buy, I'm going to get some expert advice on what kind of car I should buy. It should be the same for investors.

In the above extract, the piecemeal approach towards work and the importance of rules cumulatively translates into a professional outlook that singularly lacks an ethical compass. The analyst here shifts the onus of evaluating the nature of the professional output to the public. In doing so, he highlights an important aspect of his view of professionalism: the notion that anyone who utilizes professional output has equal if not more responsibility to ensure its content and veracity. This approach to responsibility is very different from the

expectations of the Congressional Representatives who emphasized that professional output should be created keeping in mind the interest of the large group of unorganized investors.

Social Trustee Model

(a) Low task boundedness. Unlike the expertise based model which breaks up professional work into a series of tasks, the following abstract from one of the professionals in Enron illustrates a different view of work.

> **Ms. Watkins:** Well, the Condor structure troubled me, the fact that it was off-balance-sheet troubled me, the fact that we were getting funds flow from operations, a financial performance statistic, from this structure troubled me. And while I was working in the Caribbean business unit we were instructed that we now had new targets-they were funds-flow targets, and we needed to find a way of selling our merchant assets into Condor Whitewing. It was almost like something that was on paper, not real, because the business unit continued to manage the asset, the counter party never understood that we had supposedly sold it, and there was an unspoken understanding that we could buy it back at some point in the future.

This extract is from the testimony of an accountant in Enron. It is interesting because it does not appear to be fixated on examining only a limited aspect of professional work. For one, she refers to the work the entire team is involved in, thus exhibiting awareness beyond her individual responsibility. Second, she questions the intention behind the Condor Whitewing structure and its related consequences.

One of the differences between the expertise and the social trustee model is in the inclusive view of work. Professionals in Enron exhibit another way of taking a more inclusive view of work, and that is by thinking about the risks and tradeoffs on a long term basis, as the illustration below suggests.

> Cynthia Harkness, an Enron lawyer, still at the company, described the moment when chief financial officer Andrew Fastow introduced her to a concept of monetization. The lawyer was baffled by the nerve behind Fastow's logic. She told him, "Andy, it seems to me that if you do a 10-year deal, and suck all the earnings out in one year, you will then have to keep the profit coming through years 4, 5, 6, and all the way to 10, by doing more of these deals.... How are you going to do that if the market changes? Book more deals? This is just not right, this could be fraud". She recalled Fastow looking at her and saying, "You just have to remember to keep doing more of these deals each year." **(Donovan, 2001:5)**

In the above extract the Enron attorney understands the concept of monetization but her objection is based more on the long term results of choosing this option. The consequence of monetization would mean ensuring that profit comes in at the same rate for a particular project as long as it stays operational. This is a difficult feat to accomplish for any established project, let alone a new one. The CFO's option appears to her as neither feasible nor right.
Apart from the consideration of the consequences of professional choice, professionals in Enron perceive the worth of professional work by evaluating another aspect: the relationship between intent and consequence. Compared to the expertise based model, the social trustee model of professionalism goes beyond the technical aspect of professional work and examines the real reason behind professional output.

> **Rep Greenwood**: Let me ask you this specific question. Is it your opinion that the Raptor transactions then were nothing more than sheer income statement manipulations? And if you do think that, why do you say so?
> **Mr. Mintz (Attorney and Asst. General Counsel, Enron)**: That is my opinion, and it is my opinion because true economic risk was not passed to a third party. Raptor owed Enron in excess of $700 million and there was not an outside third party that bore that loss. It was going to be borne by Enron shareholders

In the above extract, Jordan Mintz, Enron's Assistant General Counsel, raises questions about a financial structure not because of technical incorrectness, but more because of the intent with which the structure was set up. By raising the question of 'true economic risk' he ventures into the issue of accountability and the consequences of such decisions for Enron's shareholders. A model of professionalism, such as the social trustee model that relies on an inclusive view of work, the exercise of discretion, and examining the relationship between intent and consequences, does not have to rely on an easily defensible and a clearly stated target of accountability.

Target of accountability: investor centric: Compared to the rule centric approach to accountability exhibited by professionals in professional service firms, professionals in Enron view accountability as owed to a set of constituents outside of the professional-client relationship, as the following extract suggests.

> **Rep Dingell**: So, am I fair in inferring from this that their statements about the character of these devices as being of benefit to Enron were in error?
> **Ms Watkins**: Well, a benefit to Enron, if you consider that we were meeting financial statement targets that we had told investor-analysts, but you can't meet those targets falsely.

Rep Dingell: So, they were- they were essentially represented as being of benefit in the meeting of targets, which could not be met?
Ms Watkins: Yes, sir. It appears that some of these vehicles were used for financial statement manipulation.

The extract illustrates the manner in which the professional distinguishes between two separate constituents of professional work: the clients (in this case Enron itself); and investor analysts who are external to the professional-client relationship. The financial structures in Enron, designed with the input of its external counsel and auditors, were definitely helpful to the client (Enron) as they made Enron's financial state look better than it actually was, but they were *not* designed in the interests of the users of the professional output. In fact, by creating financial structures that made Enron appear attractive, there was a *deliberate* attempt to mislead the analysts and the investors. In fact, the very same professional when discussing professional responsibility goes on to suggest the following:

> Well, my understanding as an accountant is that, you know, it's an odd situation. The accounting industry is paid by public—by companies requesting their services. But your—an accounting firm is supposed to keep an eye on who is relying on their opinions. Outside investors are relying on their opinions. That's who they are here to protect. And they make an opinion that these financial statements, including the footnotes, fairly represent the financial condition of the company. (**Sherron Watkins, Accountant, Vice-President, Enron corp.)**

The above extract is one of the clearest statements of the social trustee model of professionalism that emphasizes that the outside investors need access to financial statements that represent fairly the financial condition of a company. The social trustee view of accountability is a contrast to that of the view in the expertise based model which insists that the investing public should do its own due diligence, and evaluate the nature and veracity of professional output available before taking any decision.

Comparison of the two models: Based on the above discussion, the general picture of the expertise based model of professionalism that emerges emphasizes high task boundedness, viewing conflicts as a normal process of professional work and a rule centric approach to accountability that helps in the reconciliation of seemingly opposing roles. The *expertise based model* emphasizes the centrality of rules characterized by the focus on technical correctness. Combined with the selective construal of personal responsibility, these values help to marginalize issues of intent and consequences of professional work, limit review by peers, and reduce the need for discretion and autonomy. In this model, claims to professional

status are predicated upon a command of an abstract body of knowledge that is superior to others in its application to a given set of activities and tasks, and, critically, which is allotted through mechanisms of the marketplace. Notions of disinterested service and commitment to broader ideals of public welfare are minimized. It is important to note that all professionals in the professional service firms were very consistent in their adherence to the expertise based model of professionalism. However, despite the fact that the corporate bureaucratic organization is entirely different in its set-up from the professional service firms, there were instances of professionals espousing the expertise model there too.

In contrast, the social trustee model emphasizes viewing professional output in its entirety by focusing on the way different tasks relate to each other, and by examining the relationship between intent and consequence. In viewing professional work in an inclusive way, professionals espousing the social trustee model approach accountability in a very different way. Accountability is owed more to the unorganized investors who use professional output to make investing decisions rather than to a set of rules which can be maneuvered based on the requirements of clients or the inclination of professionals. In examining the relationship between intent and consequence, professionals exercise their judgment and moral sensitivity keeping in mind the interest of constituents not directly involved in the professional-client relationship, such as the individual investors. These characteristics indicate a set of values more in consonance with the traditional model characterized by autonomy, discretion and peer review, and is much more in tandem with the expectations initially articulated by the Congressional Representatives.

More than discerning two models of professionalism, the pattern of their presence in the different organizational forms proved much more surprising. The expertise based model dominated in all of the professional service firms and was also present in the corporate bureaucratic form. The social trustee model however was present only in the corporate bureaucratic form. Table 4.1 illustrates the number of textual extracts of the expertise based and the social trustee model in the two organizational forms.

Table 4-1: Textual extracts related to models of professionalism in the two organizational forms

Models of professionalism	Attributes	Professional service firms	Corporate bureaucracy
Expertise Based Model	High Task Boundedness	53	17
	Rule oriented	41	11
Social Trustee Model	Low task boundedness	0	35
	Investor centric	0	22

As indicated above, the corporate bureaucratic form is able to accommodate both the social trustee and the expertise based model, while the professional service firm is completely dominated by the expertise based model. This finding is very interesting because it sets up two important questions:

- Why does the corporate bureaucratic form allow two models of professionalism, given that extant literature suggests that it should only or predominantly support the expertise based model?
- Why do professional service firms which are seen as professional friendly accommodate only the expertise based model?

The next section discusses why organizational forms such as the corporate bureaucracies may be better at accommodating two different models of professionalism, compared to a more informal organizational form such as the professional service firm. My analysis suggests that the manner in which professionals allude to organization specific features is a fair indicator of the way in which professionals perceive their employing organizations. This also enables an understanding of the aspects in certain forms that enable or constrain the ability to accommodate certain models of professionalism.

Models of professionalism and organizational forms

One of the broadly agreed upon assumptions in the sociology of professions is that professionals work in a self directed manner valuing peer review, discretion, and autonomy. Where such conditions are absent professionals are likely to feel stifled and experience role

conflict and strain. But in situations such as Enron, where professionals in an 'unfriendly' organization form exhibited behaviors that are labeled professional, it becomes important to understand the manner in which organizational features are being perceived by professionals working in these organizations. The concept of organizational form refers to those characteristics of an organization that identify it as a distinct entity, and at the same time, classify it as a member of a group of similar organizations (Romanelli, 1991). Extant research suggests that forms reflect the larger institutional pressures that certain sets of organizations face. These pressures lead to a pattern or configuration of organization structures and systems underpinned by specific ideas and values (Ranson, Hinings & Greenwood, 1980; Miller & Freisen, 1984; Greenwood & Hinings, 1996).

A key puzzle in this study is to understand how an organizational form such as the corporate bureaucracy with formal structures traditionally seen as being inimical to professional work, could accommodate two different models of professionalism, while a professional friendly organizational form such as the professional service firm would exhibit not only a single model of professionalism, but one that was very different from the general expectations of the public. I propose that the ability of a certain organization type to accommodate different models is explained by the role of formal structures, systems and other aspects such as supportive networks. A tabular representation of the number of extracts for formal and informal aspects in each organization form is presented in Table 4.2. Following that, different aspects of structure, systems and supportive networks are discussed in detail.

Table 4-2: Textual extracts relating to formal and informal aspects of organization forms

Organization Form	Structure		Systems		
	Policies	Centralization	Reward and Compensation	Training and Socialization.	Supportive Network
Professional Service Firms	47	12	11	27	0
Corporate Bureaucracy	63	23	13	22	17

Structure. Structure within the two different organizational forms was examined by discerning, first, the extent to which organizational policies and processes were present *and* utilized; and second, by exploring the importance of centralization within the two forms.

(i) Organizational policies and procedures

Professional Service Firms: The analysis reveals that professional service firms appear to be low on formal aspects. However, this perception is not because of the absence of formal processes or policies but more because of the manner in which professionals *perceive* these features, as the abstract below indicates.

> **Mr. Andrews (Partner, Arthur Andrews)**: Policy requires that documents should be disposed of when no longer needed-but retained when litigation has commenced or is threatened. Precisely when that occurs often will require the application of informed judgment to the particular circumstances of a given case and that may be a point on which reasonable people can differ. It also may be a point that looks quite different in hindsight than it did to people making decisions at that time.

The extract is part of a discussion focused on the destruction of Enron related documents by Arthur Andersen professionals. Professionals testifying for Arthur Andersen highlighted two key issues. First; their document retention policy was no different than the policies of other similar professional service firms. Second, document destruction was a routine and regular part of an audit process, which was stopped as soon as Arthur Andersen received a subpoena. The abstract suggests that even though there is a policy regulating retention and destruction of documents, professionals in the PSF have the option of following or ignoring them based on a specific situation.

Congressional Representatives were troubled by the timing of the document destruction, which was triggered by a copy of Andersen's document retention policy sent to the engagement team associated with Enron. It was sent to the engagement team the day Enron received the SEC subpoena. The decision to destroy Enron related documents was examined in detail by the Committee.

> **Ms. Temple**. Yes. There is a list of examples to be reported to the legal group that calls for notification. I don't believe-
>
> **Rep DeGette**. That would trigger, then, a notification such as the one that you made, I think, on October 12 in your e-mail, right? It is not just threatened litigation, is it? There are other things that would trigger Arthur Andersen to recommend retention of documents?
>
> **Ms. Temple**. The policy does require retention of all related materials if there is threatened litigation or-
>
> **Rep DeGette**. Or other situation, right? And one of those situations would be oral indications from management or owners that the firm was somehow responsible for the failure of operations or the failure to detect fraud, right? That is the-that is the third one on the list of examples of situations to be reported, right?

In this extract the Congressional Representative, using a copy of the Arthur Andersen policy, questions the destruction of Enron related documents. The Congressional Representative shows the Andersen professional clauses within the policy which serve as examples of when to retain documents. Threat of litigation and oral indication about failure of operations are instances that were eventually borne out in the Enron situation. Ms. Temple's unfamiliarity with the clauses of her organization's policy suggests that there are influences other than formal policies that guide professionals' decision-making process. In fact, from other extracts it appears that professionals in Arthur Andersen have very limited idea of what the policy really contains because of its infrequent use.

> **Rep DeGette**. Let me back up for a minute. How many times in your 2 years, roughly, at Andersen did you send memos like this to remind people of the document retention and destruction policy?
> **Ms. Temple**. I don't recall the number of times.
> **Rep DeGette**. Had you done it before?
> **Ms. Temple**. To the best of my recollection, maybe one other occasion.

Ms. Temple's admission of the infrequent use of the document retention policy is substantiated further by another Arthur Andersen partner who expressed his surprise on receiving the policy in his e-mail.

> **Rep DeGette**. Okay. Well, you had never gotten a memo like that reminding you of the policy, had you, sir?
> **Mr. Odom**. I have never gotten one with a doc. link on it like that, no, ma'am.
> **Rep DeGette**. And how long have you been with the company?
> **Mr. Odom**. Since 1969.

Both extracts bring to light Andersen professionals' unfamiliarity with organizational policies and their limited role within that organization. This is an important point because it emphasizes that the level of formality or informality cannot be inferred simply on the basis of absence or presence of policies and procedures. Unless organizational members perceive their importance, organizational forms with formal aspects can still function in a relatively informal manner.

Corporate Bureaucracy: Compared to the professional service firms, professionals in the corporate bureaucratic form tend to view their organization in a very different way, as the following extract illustrates.

> **Rep DeGette**: -- personally in accounting meetings, talking about accounting treatments of transactions. You saw the transaction sheets that the chairman showed you, the four that had

the signature line for his approval. Would it, in your experience, be like Mr. Skilling to not sign those?
Ms Watkins: No. The procedures around our approval sheets were cast in stone.
Rep DeGette: And were they used in many transactions?
Ms Watkins: Yes. Any capital expended at Enron above a certain amount had a deal approval sheet, and the procedures were very well- identified. And I never recall an instance where the approvals, indicated via the approval signature block, were not obtained.
Rep DeGette: So if someone sent those to Mr. Skilling and he didn't sign them, in your opinion, that would be intentionally?
Ms Watkins: No deal could be done without all those approvals. And quite often it was a verbal approval over the phone, and then it was always followed up by a signature.

The policies and procedures at the corporate bureaucratic form appear to be well understood and followed more rigorously than at the professional service firm. In the extract above, the routineness and the regularity with which policies are utilized for organizational tasks becomes quite evident. Unlike the professional service firms, the professional in the corporate bureaucratic form is very aware of the conditions in which the policy becomes operational.

(ii) *Degree of centralization*

Professional Service Firms. One of the substantive ways in which professional service firms appear different from the corporate bureaucratic form is in the apparent absence of a strong centralized hierarchy. Not only do PSFs appear to lack channels which could be utilized by members to voice concerns or seek guidance, there is in this organizational form a strong expectation that individual professionals are capable enough to manage highly unusual situations such as Enron's failure without guidance or direction.

Rep Greenwood. Mr. Andrews, let me interrupt you for a second. My understanding of your company's position is that on the 23rd, Mr. Duncan then set off this process, this initiation to destroy documents. But what we can't understand, what I would like to know is why in God's name, on October 23, didn't the chief counsel for your company, the top brass at Andersen, immediately send out word to everyone in the company, particularly those involved in the Enron case, to not touch documents, not shred a document? Why didn't that come down from the top immediately?

Mr. Andrews. With regard to that question, the responsibility for that rests with the engagement partner, a very seasoned, experienced individual. And we rely on the engagement partner to make that judgment, to make the judgment of what to do, as well as when to seek counsel. We did not-

Rep Greenwood. And all of Mr. Duncan's superiors in the company, including Mr. Berardino, and knowing this meltdown was happening at Enron, knowing that this SEC investigation was on, sat silently, just assuming that Mr. Duncan would do the right thing? They gave him no direction whatsoever?

Mr. Andrews. Mr. Chairman, again, Mr. Duncan had been advised of our policies in the memo on October 12. We expect our engagement partners to understand our policies and apply them.

In the above extract the Congressional Representatives are surprised by the lack of involvement and direction from the senior partners in Arthur Andersen regarding the Enron situation. Knowing that Enron was undergoing investigation initiated by the Securities and Exchange Commission, none of the senior partners came forward to offer guidance or help to the engagement team. Andersen's argument emphasized that the partners are supposed to understand the policies and implement them. Even though the lack of involvement of the senior partners at Andersen may appear surprising, in light of the expertise based model which is very task oriented and bounded, the functioning of the organization is in consonance with the model of professionalism they endorse.

Corporate Bureaucracy: The corporate bureaucratic form offers a strong contrast to the PSFs. Apart from clear and operational policies, it has a centralized set up which offers professionals the opportunity to voice their concerns through a channel that has the resources and the ability to mitigate it.

Rep. DeGette. And did you ever go to any of the board members, Mr. Winokur or others, and tell them of your concerns, that Mr. Skilling had not signed these sheets?
Mr. Mintz. I didn't, Congresswoman.
Rep. DeGette. Why not?
Mr. Mintz. In an organization like Enron, I try to work within the system and report to people who are senior to me who I felt had the direct responsibilities with the board.
Rep. DeGette. Okay. Did you ever report to your people who were senior to you of your concerns that Mr. Skilling had not signed these sheets?
Mr. Mintz. I did.
Rep. DeGette. Who was that?
Mr. Mintz. It was Mr. Buy and Mr. Causey.
Rep. DeGette. Mr. Buy and Mr. Causey, you said, ``I am concerned Mr. Skilling has not signed these sheets."
Mr. Mintz. That is correct.
Rep. DeGette. What did they tell you they would do?
Mr. Mintz. They told me to send a memo or get with Mr. Skilling and see if he wanted to get a whole packet of documents or----
Rep. DeGette. And you did send a memo, right?
Mr. Mintz. Yes, Congresswoman.

In the above extract an Enron professional who was concerned about the absence of the CEO's signature takes the initiative to inform his seniors of the problem. His seniors in turn advise him to take a certain course of action. This kind of an exchange is in contrast to the

Arthur Andersen extract where the engagement team leader was expected to take decisions completely on his own.

The extracts related to formalized policies and processes and centralization suggest that professional service firms and corporate bureaucracies differ not so much in terms of the *presence* of formal aspects but are different because of the manner in which professionals *perceive* how clear or complex these mechanisms are. Both the organizational forms had policies in place to guide decision-making but professionals in the corporate bureaucracy appear to have a clearer understanding of the manner in which these policies are to be utilized. Professionals in the professional service firms, on the other hand, appear to use policies strategically.

Similarly, both organizational forms appear to have a fair extent of centralization. For the professionals in the professional service firms, the visibility of the centralized aspect grows stronger or weaker based on specific situations. For example, during the document destruction in Arthur Andersen, there was hardly any guidance from the top management, yet as soon as Arthur Andersen received a subpoena, the top management swung into action and put four senior partners of the Enron engagement team on administrative leave and relieved two others of their responsibilities. Compared to the PSFs, professionals in the corporate bureaucracy exhibited very clear understanding of the various channels present in their organization that had the resources to mitigate their concerns.

Systems. Organizational systems such as reward and incentives, and training and socialization are indicative of the goals valued by the organization and may influence professional work and behavior.

(i) Rewards and Incentives

Professional Service Firms: The perception of the relative absence of formal structures may point to an organization with negotiable goals, but other systems within a professional service firm such as rewards and compensation are an indication of and influence professionals' perceptions of their work and responsibility.

> **Mr. Tice (Security Analyst):** With that preface, I will begin by identifying a few of the more acute conflicts. Most stem from the blurring of the lines between research and

> investment banking that I just alluded to. This blurring can be seen in a number of ways. First, an analyst's salary and bonus may be linked to the profitability of the firm's investment banking business, motivating analysts to produce favorable research that will attract and retain investment banking clients for the firm. Second, at some firms, analysts are accountable to investment banking for their ratings. Third, analysts sometimes own a piece of a company that they cover, mostly through pre-IPO share acquisitions.

In the above extract a security analyst identifies investment banks and security analysts working together as a source of conflict which may lead to the domination of certain set of goals not in consonance with a profession's public obligations. It could well be that when two groups with differing goals work together and organizational processes are geared towards rewarding one set of objectives, the other gets marginalized. A clearer statement of the result of one set of objectives valued over the other is offered by the CEO of a security analyst firm.

> **Mr. Cleland.** Well, I think I wouldn't use the word "corrupt". I would use the word "conflicted". I mean, there's nothing wrong with representing companies. The problem in the system is, is people think the system represents investors. And the structure, the economics, the compensation and the regulation is all biased toward helping company interests subordinate investor interests. That's the system.

The prevalence of the expertise model of professionalism in the professional service firm is much clearer in the above extract. Based on the discussion in the first section, the expertise based model tends to marginalize the interests of the individual investor, normalizes the notion of conflict, and elevates the market as the ultimate arbitrator of professional quality. Mr. Cleland's discussion of the structure, economics and compensation of his firm is a fairly strong statement of structures and processes within an organization that supports the espousal of the expertise based model of professionalism.

Corporate Bureaucracy: One of the main differences between the reward and compensation systems of the PSFs and the corporate bureaucratic form is in its clarity. The corporate bureaucratic form clearly privileges organizational interest over any other, something understood and apparently accepted by Enron's members, as the following extract suggests.

> **Rep Rush**: And the-most people were conscious about their upward mobility in the company, and they thought that the company would be a place to move up fairly quickly? And-is that -
>
> **Ms Watkins**: Everyone was very conscious of what they were contributing in the last six months. The performance ranking system judged you on what you contributed to the company in the last six months-no old tapes. And so-and in that sense it was very competitive.

> **Rep Rush**: And Mr. Fastow and Mr. Skilling and others could very easily manipulate that type of concern to help people to overlook some of the transgressions that we are looking into right now? Is that your opinion?
>
> **Ms Watkins**: Enron paid its people very well. The stock had been performing very well. I think there was a concern by most people that you didn't want to rock the boat.

The extract above is by one of the professionals in Enron who is discussing the compensation policy of the organization. It is interesting to note it is a system that is clear and very well understood by all of the members, whereas in the professional service firms professionals speak of the probability of assuming that the system is designed to keep public interests paramount - there is no such ambiguity in the compensation system of the corporate bureaucratic form.

(ii) Training and socialization

Professional Service Firms: In the professional service firms client interests appeared to dominate the training and socializing process:

> "As an Arthur Andersen manager," I said, "you have an obligation to every stakeholder shown here." There was general nodding of heads. "Okay," I continued, "which one is most important?" I waited patiently for someone to pipe up. But no one did. No hands, no response. I asked the question again. Eyes shifted around the room in discomfort. A few people openly turned around in their seats to see if anyone was observing the session. Again I waited. Then I spoke. "It can't be that hard to answer: to whom are you most responsible?" finally one young manager timidly raised his hand. Very quietly he said, "The partner." Most others responded the same way." What about the public investor? What about the client?" I asked. "They're important," someone responded, "but not as important as the partner." "So what does that mean?" I asked. "It means I do what my partner tells me to do," he said. "And what" I continued, "If your partner asks you to do something you think is wrong?" No one dared to breathe. "Would you do it?" Finally a timid voice spoke up: "I guess I might ask a question. But if he insisted I do it, yes, I would. Partners don't want to hear bad news." **(Toffler, 2003: 227)**

The above extract highlights the importance of and the extent of socialization which sensitizes professionals in Arthur Andersen to the objectives and goals endorsed by the partners. An important thing to note is that the socialization process trains professionals to treat the individual investor's interest as secondary; another instance that suggests that the preferred model of professionalism is the expertise based model.

The separation of the investor's interests from that of the professional and the client is more evident in the functioning of the attorneys at Vinson & Elkins, Enron's external counsel. Vinson & Elkins were asked by Enron's top management to investigate the concerns that

Sherron Watkins, an Enron employee had raised in her letter to the erstwhile CEO, Ken Lay. Even though the mandate was to examine these concerns, the lawyers at Vinson & Elkins decided to seek guidance about the extent to which they would investigate the issues raised. The terms of the investigations were decided informally between the partner at Vinson & Elkins and the General Counsel at Enron.

> ... in preliminary discussions with you, it was decided that our initial approach would not involve the second guessing of accounting advice and treatment provided by Arthur Anderson, that there would be no detailed analysis of each and every transaction and there would be no full-scale discovery style inquiry.

The rest of the investigation was guided more by client consideration than by the need to address the accounting concerns raised by Sherron Watkins and other professionals. This unbridled sensitivity to client needs to the exclusion of professional responsibility towards a broader audience disturbed Congressional Representatives.

> **Rep DeGette**. Now you did know, didn't you, that Sherron Watkins' allegations were that the accounting scandals were the problem. Isn't that correct?
> **Mr. Dilg**. She raised a number of different things in her correspondence with Mr. Lay.
> **Rep DeGette**. Right, but I mean basically she said we will implode in a way the accounting scandals and there's an elaborate accounting hoax and then her supplemental information indicated she thought there were accounting problems with a number of the transactions, most particularly Raptor, correct?
> **Mr. Dilg**. She was concerned about the Raptor transaction, primarily.
> **Ms. DeGette**. Right.
> **Mr. Dilg**. Her main concern was that Mr. Lay, in coming back in as CEO, thoroughly understand the issues he had with the business issues of the vehicles unwinding 2 years hence and the problems that might cause.
> **Rep DeGette**. If you'll excuse me, I've looked at-I assume you reviewed all of her-both her letter of concern and also the attached specific concern she raised, didn't you?
> **Mr. Dilg**. Yes, we did.
> **Rep DeGette**. Well, because she says here about Raptor, the accounting treatment looks questionable, and talks about equity derivatives. "The equity derivative transactions do not appear to be at arm's length. There's a veil of secrecy. Employees are questioning our accounting propriety" etcetera. Aren't those all issues around accounting?
> **Mr. Dilg.** Yes. All those statements relate to accounting.
> **Rep DeGette**. Did you understand what those allegations were?
> **Mr. Dilg.** We understood her base allegation to be concern about the fact that the Raptor vehicles were supported by Enron stock and that Enron had hedged investments made against those.
> **Rep DeGette**. Right, and she had specific concerns about specific transactions. Did you ever have any independent accountant look at those transactions?
> **Mr. Dilg.** We did not.

The importance of client relations within a professional service firm is indicated by the extract above, which is not surprising given that the expertise model of professionalism holds the market as the ultimate arbitrator of professional proficiency. In such a set up

clients interests would be privileged. Client influence on professional work is further illustrated by the personal experiences of security analysts.

> **Mr. Hymnowitz**: It is easy to reward favored analysts. They are given more access to management, "helped" in making earnings estimates. They'll even call you up and tell you that your estimates are too high or too low, and invite you to resorts for "briefings." And most important, their firm receives lucrative investment banking business. Companies penalize analysts who aren't sufficiently enthusiastic. Let me give you a personal example. When I was a brokerage firm analyst, I downgraded a stock. The company's chief financial officer called my firm's president to say that unless I recommended his stock, he would cease doing investment banking business with my firm, and would order the bank which managed his company's pension fund to stop doing any business whatsoever with my firm.

The security analyst's extract provides an interesting insight into the informal ways in which clients can influence professional work. In conjunction with the infrequent and discretionary use of policies and a relatively inert hierarchy, the role of informal mechanisms within these organizations becomes very prominent.

Corporate Bureaucracy: Compared to the professional service firms, the allusion in the data to training and socialization within the corporate bureaucratic form were few and pointed primarily to the culture in Enron:

> **Rep Rush**: My time is running down, but I really-I want to-if you could just explain to the committee about the culture there at Enron. It seems to me that everybody from the president to the parking lot know that there was-the parking lot attendant-knew that there was something going on there. I mean, what-explain to us about the culture that was prevalent there in the company.
>
> **Ms. Watkins:** Well, I certainly think it was fairly well known about the Raptor transactions within the global finance unit and within the business units that hedged with Raptor. .And the culture-I mean, Enron was voted most innovative. It was voted one of the best places to work. I mean, it was the job to have in Houston. The atmosphere was electric. It was fun. You were surrounded by bright people, energized - change the world. It was-you felt somewhat invincible. And, yes, people were arrogant, and it was-did have a trader kind of mentality that was sometimes tough to live with. But it was always a fun place to work.

In the above extract, the professional working in Enron describes the culture of the organization. It appears as an environment fairly consistent in being innovative and results-oriented without having any other set of expectations that muddles up the central focus. At one level the culture at Enron appears almost as strong and consistent as Arthur Andersen's, but the effect on professionals within Enron is not the same most likely because of the concurrent presence of strong formal structures.

In addition to the formal features, there are other non formal aspects of organizations that may play an important role in understanding how some organizational forms are able to accommodate different models of professionalism.

Supportive Networks. An unanticipated feature emerging from the data that shed light on the way in which corporate bureaucratic forms sustain different models of professionalism was the presence of an intra-organizational network. Enron members who were concerned about issues of accounting and financial structuring connected with others in the organization.

> **Rep DeGette**: Can you tell me how widespread the concern was?
> **Mr. Mintz**: The Enron global finance staff knew about it, and various business units that had sold assets to Raptor knew about it. There were whole sections of Enron—the pipeline group, the trading group—that had no idea about it. But in some groups it was widespread knowledge.
>
> **Rep DeGette**: Well, what about your group? Did people talk about this commonly? How many people are we talking about?
> **Ms Watkins**: I think a fair number. I mean, one of the things that I asked Vinson &Elkins to do was to look at—a survey had been conducted by Mr. Lay over the Labor day weekend, and I knew of at least a dozen people who had typed in serious concerns about our accounting. Well, I can share Jeff Donahue, who was managing director in charge of corporate development. Kim Detling (sp), a managing director in corporate development. Michelle Nezzy (sp) Marvin one of the business unit people who hedged assets with Raptor.

The above extracts suggest that many members shared concerns about accounting and the structuring of the special purpose entities. As all of them shared a common concern about the effect of these problems on Enron, they were able to create a network that provided credibility and support to each other.

> **Mr. McMahon.** I did. I called Mr. Lay and explained to him that although I was unaware of any of the facts in her letter, whether they had merit or not, I did validate that Ms. Watkins was in fact a reputable source and employee and she should be listened to with----
> **Chairman Tauzin.** So you did vouch for her to Mr. Lay?
> **Mr. McMahon.** That is a fair assessment.

This intra-organizational and almost guerilla-like network enabled professionals to continue in the organization whilst voicing their concerns. Some of respondents were also in touch with professionals outside of the organization who helped them corroborate the soundness of their concerns. For example:

> **Ms Watkins**: Well…that is why I called Mr. Hecker in Andersen. I was about to meet with Mr. Lay, and I thought—well, I called him, but since I had not been in accounting for a while to say, you know, could this ever be okay? And he said it didn't sound right. And his words to me were, Sherron, any accounting treatment must be clearly defensible when fully exposed, you are probably correct, and you should go and see Mr. Lay.

To a large extent the intra-organizational network in Enron was sustained and facilitated by the separation in the lines of authority in the different divisions, and by options of shifting within different divisions each with specificity and clarity in job responsibilities.

> **Mr. Mintz**. I came into the job at Global Finance in October 2000. Prior to that, I was a tax attorney for 18 years. I met with my predecessor for 2 days in making the transition. He brought me up to speed on what was going on, reviewed the employees in the Legal Department, et cetera, and never mentioned LJM; got into the office, opened up the files and a substantial amount of documentation, deal approval sheets that…
> **Rep DeGette**. And you went to Mr. Derrick, and you told him about the concerns you were seeing, correct?
> **Mr. Mintz**. I was bringing--I advised him on what was going on the 20th floor.
> **Rep DeGette**. When was that?
> **Mr. Mintz**. I think our first formal meeting was in March of 2001.
> **Rep DeGette**. Okay. And you told our committee staff that when you told him about all of this, he was just sort of poker-faced, didn't say anything, right?
> **Rep. Burr**. Am I safe to assume from that answer that the points that you might have raised with Mr. Derrick were on deaf ears?
> **Mr. Mintz**. I don't think he appreciated the dysfunctionality that I observed.

The kind of mobility that is possible between different divisions of the corporate bureaucratic form is absent within professional service firms. It is probable that professionals who move from division to division are more likely to adhere to a more traditional set of values rather than imbibe new ones wherever they go. In doing so, they may be more sensitive to shifts in values and goals between different departments.

Also for professionals in Enron, the repercussions of behaviors which the Congressional Committee labeled 'professional' such as raising issues, complaining to seniors and even whistle blowing were limited. Professionals who raised concerns protected themselves by asking for a transfer to another division or by getting transferred as a consequence of complaining, as the following abstract indicates.

> **Ms Watkins:** I met with Mr. Lay on the afternoon of Wednesday, August 22nd, 2001. The meeting lasted just over one half hour. I provided him with five memos I had drafted to help explain the problems facing the company. Additionally, I provided Mr. Lay an analysis of the Raptor entity economics and a presentation prepared by Enron's risk assessment and control group. I urged Mr. Lay to find out who lost that money. If he discovered that this loss would be borne by Enron shareholders, via an issuance of stock in the future, then I thought we had a very large problem on our hands. I gave Mr. Lay my opinion that it is never appropriate for a company to use its stock to affect its income statement. At the conclusion of the meeting, Mr. Lay assured me that he would look into my concerns. I also requested a transfer, as I was uncomfortable remaining as a direct report to Mr. Fastow.

Transfers were not always a choice, as in the above extract. In some cases professionals who were seen as uncooperative were transferred as punishment.

> **Rep. John.** Okay. And, finally, we were getting down to Mr. McMahon's--to maybe the crescendo of this meeting he had with Mr. Skilling about what all happened. And as you walked out, he said that he is going to try to fix this. But isn't it true that you also shared a lot of the concerns with Mr. Causey, Mr. Buy, Mr. Lay and Mr. Sutton, and not one of them helped you or gave you advice, other than maybe just, ``Get out of the way.''
>
> **Mr. McMahon.** Actually, the process was a little bit different. I actually had a long discussion with my wife before I even walked into Mr. Skilling's office, because I knew the potential ramifications. Mr. Fastow, actually, did not suggest I take a new job; in fact, quite the opposite. About a week or two later, he called me in and suggested that he was unclear whether he and I could continue to work together.
>
> **Rep. John.** Mr. Fastow.
>
> **Mr. McMahon.** Mr. Fastow, who was my boss. It was hours after that meeting when Mr. Skilling advised me that he thought there was a much better job in the company for me and that I should seriously consider taking it.

The intra-organizational network and the mobility between divisions made certain that professionals who disagreed were supported by others elsewhere in the organization. The network also ensured that dissent and resistance could be voiced, addressed (even if superficially), and accommodated within the organization.

This supportive intra-organizational network was present *only* in the corporate bureaucracy. Its complete absence in the professional service firms is surprising but is more readily grasped when one considers the interaction between aspects of organizational form and models of professionalism. Up until this point the discussion of the results was geared towards understanding how the two organizational forms differed from each other. These differences help in examining why one (the corporate bureaucracy) may be better at accommodating multiple models than the professional service firms.

The results suggest that PSFs work with an uneasy balance between formalization and professional autonomy. There are enough formal processes and policies present within PSFs to guide professional decision making and work but their use is discretionary. However, it is important to understand that this discretion is not the same as the untempered autonomy eulogized by the sociology of professions literature. As was indicated by the results from the previous section and Table 1, PSFs strongly endorse the expertise based model of professionalism. Its focus on task boundedness and outcomes influences the *nature* of

autonomy that professionals in this organizational form posses. In addition, the present section suggests that compensation and training not only reinforce outcome oriented work but also encourage professionals to identify very closely with their employing organization. This harmonious blend of core characteristics of the expertise based model along with the *discretionary* use of policies and systems creates an environment for the continued dominance of the expertise based model within the PSFs.

The corporate bureaucratic form presents a different scenario. The extracts from the section on centralization and supportive networks indicate that the corporate bureaucratic form is separated into clear divisions, each with its separate line of authority. Here, groups of professionals are scattered around the organization and are outnumbered by their non professional colleagues. In such situations professionals are likely to be guided by two key motives: first, to differentiate themselves from their non professional colleagues; and second to ensure that they maintain control over the content and process of their professional output. The social trustee model becomes attractive as a means for differentiating themselves from others. The core characteristics of the social trustee model are consistent enough to be carried across different organizations without having to familiarize or completely embrace the values of each organization or division in which they work. Formal aspects become important because familiarity with policies and procedures help in monitoring control over their work and output. At the same time, a centralized set up ensures that in case of problems, professionals have access to people who can mitigate those issues. Another distinctive feature of the corporate bureaucracy is the presence of in-house professional departments, which research suggests closely resembles PSFs (Wallace, 1995) and interacts with them on a regular basis. These in-house professional departments are then more likely to be amenable to accommodating the expertise based model of professionalism, leading to the distinct possibility of the corporate bureaucratic form accommodating *both* the social trustee and the expertise based model.

Organizational Forms and Professional Behavior

Much of the previous discussion focused on explaining why some organizational forms are more partial towards a particular model of professionalism. I examined organization specific features that enable corporate bureaucratic forms to accommodate different models of

professionalism. Therefore, the next step is to understand how certain behaviors were facilitated by unique characteristics of organizational forms. In this section I focus on behaviors which Congressional Representatives termed 'professional'. These behaviors involved instances of professionals highlighting the discrepancies within the work process, taking autonomous decisions to examine and probe their concerns in detail, supporting other professionals with similar concerns, and sometimes resorting to a variant of whistle blowing within the organization.

The previous section established that organizational forms with clear, routinized formal policies and processes enable the accommodation of multiple models of professionalism. Their non compliance serves to signal potential problems within the system.

> **Rep. DeGette**. Now, you were very concerned that Mr. Skilling had not signed those sheets, correct?
> **Mr. Mintz**. From the beginning of the job, I was very concerned, as I did my due diligence, that the policies and procedures that the board had put in place weren't being----
> **Rep DeGette.** Now, wait a minute. You were concerned that Mr. Skilling had not signed the sheets, and in fact you tried to get him to sign the sheets from time to time, even writing him a memo.
> **Mr. Mintz**. That requirement was part of the policies and procedures.
> **Rep DeGette**. And you tried to get him to do it, yes or no?
> **Mr. Mintz.** That is correct.
> **Rep DeGette.** Thank you. And did Mr. Skilling ever sign the sheets, that you know of?
> **Mr. Mintz**. I don't think so.

The above extract suggests that when these organizational policies are breached they alert people about impending problems. Professionals who ascribe to the social trustee model of professionalism then try, through the available channels, to get the problems rectified. In some cases, such as in the excerpt below, they decide to take autonomous action.

> **Rep. Burr**. Enron hired outside counsel through you or you personally hired outside legal counsel?
> **Mr. Mintz.** I hired outside legal counsel on behalf of the company as its client.
> **Rep. Burr.** On behalf of the company as its client. And your primary reason for that was what?
> **Mr. Mintz.** As I mentioned before, this Enron/Wind deal concerned me because of the magnitude, and it was different than apparently the transactions that were engaged in before LJM. Also the issues regarding some of our disclosures continued to gnaw at me, and I wanted somebody to take a fresh look at that.
> **Rep. Burr**. Who above you in Enron management did you share with the fact that you had hired outside counsel to look into this?
> **Mr. Mintz**. At that time, nobody, Mr. Congressman.
> **Rep. Burr**. You would have answered to Mr. Derrick at that time?
> **Mr. Mintz**. On the legal side, that is correct.

In this instance when going through the system did not work, the professional decides to take an independent decision to hire a law firm that has no connection with Enron. In a way, the opportunity of taking such an action was available only because there were available and established channels that substantively failed to address the concerns of the professional. In fact, most of the professionals who espoused the social trustee model of professionalism took the same route - first utilizing available resources and if that did not work, taking an independent autonomous decision.

> **Rep Tauzin**: Now, did you tell him that in fact some of the materials had come from his own shop?
> **Ms Watkins**: No, but I just told him I had some memos that I wanted to fax him, and have him look at.
> **Rep Tauzin**: Which-did you identify those memos or explain to him what they might say or -
> **Ms Watkins**: I told him I was very concerned about the Raptor transactions, that we have very large accounting issues, and that it was not appropriate to be backstopping these Raptor losses with Enron stock.
> **Rep Tauzin**: So you offered to send him all this. What was his response?
> **Ms Watkins**: He said he'd rather not see it.

In this extract the deliberate refusal of the person up in the hierarchy to address the concerns of the professional motivates her to take the initiative to send an anonymous mail and then subsequently ask for a meeting with the CEO Ken Lay.

> **Ms Watkins:** On August 14th, 2001, I was informed of Mr. Skilling's sudden resignation, and felt compelled to inform Mr. Lay of the accounting problems that faced Enron. I sent Mr. Lay an anonymous letter on August 14th, 2001. On Monday, August 20th, 2001, Mr. Lay's assistant scheduled a meeting for me to meet with Mr. Lay that following Wednesday, August 22nd, 2001. My main point to Mr. Lay was that by this time Raptor owed Enron in excess of $700 million under certain hedging agreements. My understanding was that the Raptor entities basically had no other business aside from these hedges; therefore, they had collectively lost over $700 million. I urged Mr. Lay to find out who lost that money. If he discovered that this loss would be borne by Enron shareholders, via an issuance of stock in the future, then I thought we had a very large problem on our hands. I gave Mr. Lay my opinion that it is never appropriate for a company to use its stock to affect its income statement.

The professionals who discuss their concerns justify their actions based on a few key points. First, they use the social trustee model to frame their concerns. For example, Mr. Mintz finds the conflict of interest in certain financial structures disturbing and hires a law firm completely independent of Enron to examine the consequences for the organization. This is in complete contrast to the expertise based model of professionalism which tends to see conflict as a normal aspect of professional work. In Ms Watkin's extract, she focuses on the

interests of the shareholder, who in the expertise based model of professionalism gets excluded from the interest of the professional-client relationship. Second, this group of professionals utilizes the formalized aspects of the organization to voice their concerns and then take autonomous action. In doing so they also they signal commitment to the continuance of the employing organization.

In contrast, the professionals at the PSFs not only tend to espouse only the expertise model, but they also lack the resources, such as the formal structures, that make it possible for the professionals in the corporate bureaucratic form to not only voice their concerns but also shield themselves from the negative repercussions. Though I could not find instances of professionals in most professional service firms taking similar initiative and continuing to be a part of the organization, there were rare instances of professionals in Arthur Andersen who voiced concerns but were shunted out of the organization, as the following extract illustrates:

> "There were other warning signs. Carl Bass, a member of Andersen's Professional Standards Group- the group that is supposed to oversee accounting decisions- had been removed from working on the Enron account in early 2001after he objected to some accounting practices…and finally left Andersen. **(Toffler, 2003: 176)**

The above extract is an example of a professional who may endorse the social trustee model but does not have the resources within the employing organization to voice his concern *and* continue to be a part of the organization. In organizations where the prevalent mode of control is through consultation and informal processes, there is less of likelihood for dissent to occur.

> **Rep Stearns**. Is it true that you told our committee staff that some clients in the past had been upset that old or extraneous documents had been unnecessarily maintained and discovered during IRS and SEC inquiries? I mean, our staff indicated that you told them that.
>
> **Mr. Odom**. That's correct.
>
> **Rep. Stearns**. Mr. Odom, I just-as I understand it, you have been relieved of your duties. Is that true?
> **Mr. Odom**. I am no longer the practice director for the Gulf Coast market, sir.
> **Rep Stearns**. And when did that change occur with your job description, or when were you relieved of that duty?
>
> **Mr. Odom.** It was announced in the same press release where Mr. Duncan was discharged…I asked what the reason was, and I was told the firm felt they needed to make some bold moves to regain confidence in the Houston community.

> **Mr. Andrews**. Since I obviously was involved in those decisions, I'm probably more appropriate to answer it, if you will allow me to... This (relieving the engagement partner of his duties) was a judgment, we made that collectively; the management changes we made, we believed as an organization, were changes we needed to make to rebuild the confidence.

Although this extract does not directly suggest that professionals are punished for voicing opinions contrary to the organization's interests, the Andersen partner is not able to create a strong enough argument defending Arthur Andersen's decision to relieve an Enron engagement partner of his responsibilities.

The present section was intended to demonstrate that professionals inclined to behave 'professionally' are enabled by access to two key resources: espousal of the social trustee model and being part of an organization that has features to sustain different models of professionalism. It is possible that there may be professionals espousing the social trustee model within professional service firms, but the lack of established channels of communication, formalized processes and policies and separate divisions constrain the expression of that model. At the same time it is important to remember that the corporate bureaucratic form, by virtue of its formalized nature, can accommodate both the social trustee and the expertise based model of professionalism. Therefore, professionals in corporate bureaucratic forms are more likely to be able to *choose* the model they want to adhere to and exhibit 'professional' behavior.

Discussion

The results in the previous section suggest that several factors influence the ability of organizational forms to accommodate certain models of professionalism.

Organizational Structure

Corporate bureaucracies are generally divided into different departments and divisions, each with its own clear line of authority. In addition, corporations such as Enron also have large in-house accounting and law departments which are relatively decentralized. A substantive separation between different units makes it more likely for diverse sets of values to be

'scattered' around in this organizational type. The possibility of encountering different sets of values increases further when the recruitment process is taken into account.

Many of Enron's professionals such as Sherron Watkins, Jordan Mintz, and Cynthia Harkness worked in different organizations before working for Enron. In fact, some of the professional's testimonies suggest that when new divisions were set up in Enron, many members from other different department were brought together along with new members recruited from other organizations. Thus the ongoing recruitment of new personnel from outside and the existence of different professions and occupations within the same organization create a diversity of perspectives.

The size and diversity of occupations and professions within corporate bureaucratic forms leads to professionals and non professionals working together on a consistent basis. In such situations professionals are more likely to make an effort to ensure that their area of expertise is not encroached upon. In order to do so, they are more likely to adhere to a set of values that can be transferred within and between organizations. The social trustee model of professionalism appears to be one such value set. The analysis shows that the social trustee model is endorsed strongly by the professional associations and is also widely recognized by the broader audience such as the investing public. Core characteristics constituting the social trustee model include privileging investors' interests and exercising moral sensitivity – values that are beyond individual and organizational interests. In embracing the social trustee model of professionalism, professionals increase the probability of ensuring control and discretion over their work. Espousing these values also enables professionals to exhibit specific behaviors such as voicing dissent and whistle blowing, which under regular circumstances could signal a lack of commitment to the employing organization.

Enron also had large in-house law and accounting departments which were more decentralized compared to its other divisions. The data suggests that much of the structuring of financial deals and accounting decisions were a result of collaboration between the in-house accounting and law professionals and the external auditor and counsel. The regular interaction between the in-house professionals with professionals in the large PSFs increases the probability that the organization is exposed to the model of professionalism endorsed by

the large professional service firms. In addition Enron's long and close relationship with its external auditors (Arthur Andersen) and external counsel (Vinson & Elkins) led to a number of members coming from those professional service firms to Enron's accounting and law department. For example, Enron's former general counsel was a partner in Vinson & Elkins for twenty years before moving to Enron. The influx of senior professionals in senior positions increases the possibility of the corporate bureaucratic form accommodating an alternate model of professionalism.

In case of the professional service firms, professionals constitute the large majority of the workforce and are the ones directing organizational goals and objectives. The data suggests that many of the professionals in large professional service firms worked for a very long time in the same organization. For example, one of the Arthur Andersen partners put on administrative leave, Mr. Odom had been part of the same organization since 1965. Further, as professional service firms are organizations owned and managed by professionals, they do not have the same extent of diversity in terms of professionals and non professionals compared to the corporate bureaucratic form. Therefore there is a greater potential for such organizations to support only a specific repertoire of values. This leads to the first proposition:

> *Proposition 1:* Organizational forms vary in their ability to accommodate multiple models.

In the corporate bureaucratic form, the presence and routinized use of policies and procedures are designed to substantively manage diverse groups of professionals and non professionals. Because there is clear understanding of the conditions under which policies become operational, the breach of policies can signal potential problems. For professionals who subscribe to the social trustee model of professionalism, such breaches can serve as triggers for initiating remedial actions. The routinized use of policies is supported by an active centralized authority which provides a channel for professionals to voice their concerns and ask for corrective measures. Most professionals in Enron who endorsed the social trustee model initially used the 'system' (i.e. approached their seniors and informed them of their concerns). In cases where the immediate senior was a non professional

(especially in the case of professionals who worked directly under Andrew Fastow, the Chief Financial Officer, Enron), professionals strongly evoked the 'trusteeship' values of their profession when voicing dissent. Doing so enabled them to object on the basis of a value set beyond individual and organizational interests.

In contrast the picture that emerges from the PSFs is quite different. It initially appears that PSFs are an informal organizational form but the data shows that most have policies and procedures in place. It is the frequency and the mode of utilization that is discretionary. Senior partners in Arthur Andersen insisted that the normal way of functioning in their organization was through consultation and advice but there was a clear contradiction in what they claimed and what emerged. As Congressional Representatives asked the partners about the Enron related investigation in Arthur Andersen they had very little idea of who had been interviewed and what information had come out as the result of this investigation. On being asked how often engagement partners meet with senior management, Andersen suggests that they expect senior engagement partners to take their own decisions. A similar picture of professional work focused on individual tasks and responsibility emerged in the security analyst firms as well. This apparent contradiction can be reconciled to a large extent when the dominance of and preference for the expertise based model in this organizational type is taken into account. As discussed earlier, the expertise based model views professional work as a series of tasks handled independently by individual professionals who are liable only for the assigned aspect of work. Given that professional service firms are largely owned and managed by professionals there would be a greater likelihood of a shared understanding of organizational goals and objectives.

Seen in this light, policies around work played a different role in the PSFs. For example Arthur Andersen's official document policy allows for document destruction but at the same time has clear clauses that highlight situations that should trigger document retention. However, Andersen's partners highlighted the uncommonness of the actual use of the policy. Another senior partner testified his surprise on receiving the policy as an e-mail attachment. Further, it came to light that some clients who were being investigated had expressed displeasure at the length of time that documents were retained. It appears then that the policy is followed more in its neglect than use. The rhetoric of company policy

serves the dual purpose of legitimating document destruction as a sound audit practice, and as a way to help clients out, thus highlighting its potential to be client centric. Ambiguity in policies and processes is helpful in many ways. It helps in maintaining the semblance of avenues to exercise discretion and autonomy, enforcing and endorsing a preferred model, enacting control through informal means; and assisting professionals in taking a more client centric view of their work. Informal control ensures that professionals' appropriateness of choice can be rewarded or punished through means other than organizational routines and procedures.

> *Proposition 2(a):* Organizational forms where formal features are *perceived* to be important and *utilized* in a consistent manner on a regular basis are more likely to accommodate competing models of professionalism and display the social trustee model.
>
> *Proposition 2(b):* Organizational forms where the formal structures are seen to be utilized *strategically* to attain organizationally sanctioned objectives are more likely to endorse a single model of professionalism

Organizational Systems

One of the key factors that help in explaining the difference in the ability of the two organizational forms to accommodate different models of professionalism is the rewards and compensation system. In the PSFs there is a distinct disconnect between the criteria of compensation for professionals and their discussion of their social obligations. This is most evident in the extracts of the security analysts. Some of the security analysts highlighted the manner in which their compensation is linked to the employing organization's financial well being. However, there were others who suggested that the investing public was mistaken in thinking that the structure and economics of such firms would allow them to be sensitive to social responsibilities. The commercial pressure that professionals in PSFs face, in that they are responsible for their organization's continuance and revenue generation, is likely to be one of the reasons for preferring the expertise model of professionalism. The expertise based model is attractive because it contains elements of both social trustee and commercial concerns. Within the expertise model, command over an esoteric knowledge base gets translated as technical superiority, giving credibility for its ability to achieve a desired end

(Koehen, 1996). A public service ethos gets morphed into a client-focused orientation. Thus the demonstration of technical expertise in achieving client desired ends consolidates a PSF's reputation as an expert and ensures its commercial survival.

The context of non-PSF, bureaucratic organizational forms such as Enron is quite different. These organizations have clear goals and objectives that give preference to revenue generation and organizational continuance. Compared to PSFs professionals in large corporations are not solely responsible for contributing to organizational survival or revenue generation. Their organization consists of a large number of non-professionals. The social trustee model is more attractive for professionals because it emphasizes values and goals that enable them to appear different from their non-professional colleagues. At the same time professionals in both organizational forms interact with each other. In doing so, professionals in the corporate bureaucratic forms have access to the expertise based model. Therefore, for professionals in corporations, the repertoire of acceptable actions increases significantly with access to multiple models. In situations where the employing organization's goals are clearly in conflict with professional training and values, these professionals have the *choice* to use the social trustee model of professionalism and privilege their professional values.

> *Proposition 3(a):* Organizational forms where professionals are solely responsible for the organization's survival are more likely to endorse the expertise based model.
>
> *Proposition 3(b):* Organizational forms where professionals are not solely responsible for the survival of the organization are more likely to accommodate and display both the social trustee and the expertise-based model.

The results suggest that training and socialization in large PSFs is geared towards privileging organizational goals and objectives. For example, extracts from the accounting and law firms suggest that partners' opinions and client interests take precedence over societal obligations. Organizational self interest in the PSFs is indicated more strongly by the difference between the model of professionalism that professional associations appear to endorse (social trustee)

than that endorsed by the large accounting, law and security analyst firms (expertise based model).

Moreover, Andersen's dismissive attitude towards the AICPA code of ethics indicates the redundancy of the professional association for a large PSF. This difference in the espoused models suggests that large PSFs are likely to socialize their professionals in a specialized and regimented manner. The testimonies of the professionals in the large PSFs also indicate that a large proportion of professionals trained within these organizations are likely to continue with them because of their specialized training. With time it becomes more likely that the organization will become their primary reference community. In an environment dominated by professionals who share a particular conception of professionalism reinforced by the reward and compensation system, and governed primarily through informal means such as mentoring, the probability of accommodating and expressing a competing model of professionalism, such as the social trustee model is extremely low.

Compared to the PSFs, the corporate bureaucratic form does not influence its professionals in the same manner. The results suggest that the culture in Enron was almost as strong as in the large accounting firm, yet instances of both the expertise based and the social trustee model were present there. Two key reasons moderating the effect of culture are the organizational set up with clear divisionalized structures with their own line of authority, and the constant recruitment of new personnel and transfer of old ones between departments. Both these reasons make it less likely for informal aspects to become strong enough to support only a single model of professionalism

> *Proposition 4 (a)*: The stronger the presence of internal training, socialization and compensation systems, the more likely it is for an organizational form to endorse a single model of professionalism.
>
> *Proposition 4 (b)*: The weaker the internal socialization and greater the influence of the formal structures, the greater the likelihood of an organizational form harboring and expressing competing models of professionalism.

Supportive Networks

Finally, a unique feature, an intra-organizational network, was discerned in the corporate bureaucratic form. This supportive network included professionals endorsing the social trustee model. The concerned professionals would get in touch with other professionals who had similar issues with the financial structures and accounting choices and then voice their dissent. Connecting with other professionals achieved two objectives. First, they were able to able to gain additional information. Second, the other professionals provided credibility for them and the issues they raised. For example, when Sherron Watkins decided to talk to Ken Lay, the CEO of Enron about her concerns regarding accounting choices, she was supported by Jeff McMahon, another senior professional who shared her concerns. It is important to note that there were negative repercussions to exercising dissent. Some professionals were transferred to other departments, some others asked for transfers. Even though they were in different divisions and under different lines of authority, they continued to be part of Enron, endorse the values of the social trustee model, and take initiative to highlight their problems.

There was no such instance of an intra-organizational network within any of the professional service firms. Based on an earlier discussion which suggests that PSFs are strongly inclined towards the expertise model of professionalism which is inculcated, maintained, and reinforced through predominantly informal means, it is less likely that professionals in this organizational form will have access to a competing model of professionalism.

> *Proposition 5(a):* An intra-organizational network maintained by professionals who share concerns, and sustained because of the formalized nature of the organization makes it more likely for competing models of professionalism to coexist and enables the expression of the social trustee model.
>
> *Proposition 5(b):* Absence of routinely utilized formal structures and predominance of informal forms of governing makes it less likely for an organizational form to have a network that supports a competing model of professionalism.

Models of professional behavior, organizational forms and professional space

To recapitulate, the results suggest that organizational forms such as the PSFs are seen as professional friendly because of their ability to combine organizational imperatives of revenue generation and continuance with professional values. The endorsement of the expertise based model enables this amalgamation. The apparent lack of formal structures, the insistence on working through consultation ensures enough ambiguity to maintain and reinforce the preferred model using informal processes. The results also suggest that organizational forms with formal structures such as large corporations or bureaucracies have clear consistent mechanisms in place to manage both professional and non-professional members. The structures ensure that professionals have access to multiple models of professionalism. Therefore, in the case where organizational goals are in conflict with professional values, professionals who endorse a model that is *different* (not opposite) from the organization are more likely to behave 'professionally'.

The choice of a particular model is influenced by the context of the organization. All professionals have to be aware of commercial pressures, but for professionals in PSFs, this pressure is stronger because they are solely responsible for their organization's revenue and continuance. As mentioned earlier the expertise based model enables professionals to reconcile commercial pressures with professional obligations. Further, large PSFs have career screens such as 'up or out', which perpetuate homogeneity and conformance by ensuring that those who 'fit' are retained. This increases the commitment to and strength of the organizational ideology. Thus commitment to an expertise based model along with a strong culture merges organizational and professional commitment seamlessly.

The contexts of non-PSF, bureaucratic organizational forms such as Enron are quite different. These organizations have clear goals and objectives that give preference to revenue generation and organizational continuance. Policies and structures are designed to manage these goals and expectations. However, compared to PSFs, professionals in large corporations are not solely responsible for contributing to organizational survival or revenue generation. They are more likely to endorse the social trustee model in order to differentiate themselves from their other non professional colleagues. At the same time, interacting with professionals from the PSFs gives them access to the expertise based model. Therefore, for professionals in the corporate bureaucratic form, the repertoire of acceptable actions increases significantly with access to multiple models. The availability of the opportunity and

the ability to manage and maneuver organizational and professional pressures by choosing between different models of professionalism is termed as *professional space.*

Professional Space

Professional space is the ability of professionals to negotiate organizational goals and professional values based on situational demands. Professional space can be literally imagined as the space to maneuver organizational or professional prerogatives without giving up either one. The concept of professional space is based on two core ideas. First, different groups of professionals have access to different models of professionalism. Second, some organizational forms can accommodate multiple models of professionalism and are more likely to enable behaviors termed 'professional'. Features of the organizational form that enable multiple models to exist also help professionals successfully negotiate and reconcile organizational concerns and professional values. I suggest that this kind of professional space is more likely to be present in organizations where professionals have access to multiple models. Thus, the final set of propositions:

> *Proposition 6(a)*: Professional space is more likely to be available to professionals in bureaucratic forms, such as corporations rather than professionals in PSFs .
>
> *Proposition 6(b)*: Professional space is more constrained for professionals in PSFs rather than professionals in bureaucratic forms, such as corporations.

Conclusion

The concept of professional space is interesting because it explores into the interaction between professional behavior and organizational context. Professional space can be literally imagined as the space to maneuver organizational or professional prerogatives without giving one up. There is one key feature that constitutes professional space. In order to privilege either professional norms or organizational values, both have to be demonstratively different, i.e. professionals in an organization should have access to an additional model-the model that makes them an agent of a set of principles that are valued beyond the self interest of an employing organization. From this we infer that organizational forms that accommodate multiple models are more professional friendly for they enable the expression

and assertion of professional space. The role of organizational contexts and the models they value becomes critical in understanding why access to multiple models does not create conflict. When employing organizations choose to prioritize a particular model, it may affect the access to other models for its professionals. Professionals in large PSFs reconcile commercial and professional concerns by endorsing the expertise based model which has elements of both-the traditional social trustee model of professionalism and commercial concerns. One result of adopting this model is that the commercial and professional are no longer separate. In other words, in reconciling two seemingly opposing pressures and coming up with a model of expertise, there is little space for an additional model or the 'other'. This combined with the internal processes of socializing and mentoring creates a cohesive blend of organizational and professional values. Professionals in non-PSFs do not experience commercial pressures to the extent that professionals in PSFs do. While they have access to the expertise based model of professionalism they also have access to the social trustee model by being part of the larger professional community. Espousing the social trustee model also serves another strategic purpose. It enables them to distinguish themselves from other organizational members and use their professional agency to negotiate terms and content of their work. Professional space, though largely delineated by access to different institutional models which depend on the organizational form professionals are in, is not solely structured by them.

Some of the important variables that affect professional space are factors such as training and socialization, compensation and reward systems and criteria for promotion, all of which contribute to give an organization a distinctive way of viewing itself. Sudden changes or crises situations that organizations may experience are other factors that affect professional space. A temporal view of professional work in organizations would show that professionals are not always in conflict with the employing organizations. Specific situations such as sudden changes or crises, like Enron, cause organizational imperatives and professional values to diverge considerably. In such situations, professionals in large PSFs are constrained, first because they do not have access to an additional or a more traditional model (the social trustee model). Also with an organizational culture that tends to promote conformance, their access to professional space is further restricted. In contrast to professionals in large organizations the presence of multiple models (i.e., the choice of

endorsing a more traditional model of professionalism and being part of different communities) enables them to have more professional space.

This study makes two important contributions to the sociology of professions literature. It highlights the need to move beyond the assumption that professionals share a common model of professionalism and it acknowledges that organizational forms that professionals work in interact with and influence notions of professionalism. I suggest that the assumption of a common model of professionalism and a lack of focus on the interaction between models and organizational form contributed to reinforcing the notion that some organizational forms are unfriendly for professionals. More attention to models of professionalism and the variety of organizational forms that professionals work in changes the picture and offers a persuasive explanation for the spate of professions related scandals. While this study examines large PSFs, smaller and mid-sized PSFs face different kind of pressures and have unique set of relationships with client, professional associations and the professional community. It is very likely that the creation and assertion of professional space follows a different dynamic. One of the limitations of this paper has been my inability to examine in detail how different professions affect professional space. For example, one of the core values of law is 'advocacy' while that of accounting is 'independence'. It would be interesting to explore how difference in core values of professions affects the assertion of professional space.

Post Enron, the passing of the Sarbanes Oxley act severely limits the range and scope of services that audit firms can offer to their clients. One could argue that the Sarbanes Oxley act takes care of the weaknesses that I point out in this study. I think that Sarbanes Oxley sets up new issues that make the concept of professional space even more promising. First, Sarbanes-Oxley has created greater stratification in the field than ever before. Compliance requirements dictate that only an audit firm that has the resources and training for Sarbanes Oxley compliance can service firms of a particular size. Therefore there is a greater stratification between smaller and larger client and audit firms, which will likely modify expectations of professionalism in different ways. Second, Sarbanes Oxley compliance requirements have forced large audit firms to increase policies and procedures within the organization. But as this study shows, policies and procedures can be meaningless if not

complemented by organizational values. It would be interesting to explore how new procedural requirements have influenced the exercise of professional discretion. Finally, Sarbanes Oxley has increased the liability of client firms in cases of fraud. This is in contrast to an earlier situation where clients were seen more as partners and social relations may have influenced professional decisions. In the post Sarbanes Oxley scenario, both client firms and PSFs have to undertake the role of vigilantes. But given that professional-client relationships thrive on trust, it would be interesting to explore the mechanisms that evolve to buffer the need to be on constant alert.

This study tried to highlight that professional space as a concept is much more than just an exercise of individual discretion. It is affected by field level dynamics such as organizational forms endorsing certain models and hence restricting access to some, organization specific features like reward and compensation systems and organization culture, and professionals' involvement with the professional community.

Chapter 5
Professional and Client Relationships

Overview

Chapter 2 provided a discussion of the literature of professionals in organizations and professional behavior. It highlighted the importance of understanding professional behavior as a negotiated set of standards between three groups: the professionals (and the organizations they work in); the clients; and the public. This chapter provides an overview of another important variable influencing professional behavior – the professional-client relationship.

The objectives of this chapter are twofold. First, I review the insights offered by the existing literature to examine whether it adequately explains the failure of Enron where prestigious professional service firms were investigated for colluding with their client. Second, in order to gain a richer understanding of this event I review the existing literature and suggest using additional insights from other theoretical perspectives such as resource dependence and organizational fields. To that end the chapter is organized as follows: the first section introduces the concept of client capture, which connects professional-client relationships to professional behavior. A review of the literature that has focused exclusively on professional-client relationships is followed by the next section, which discusses the different streams in that research. Subsequent sections will highlight the problems in the literature, advocate using insights from resource dependence theory, and utilize the concept of organizational field to examine the influence of professional-client relationships on professional behavior.

Introduction

A central variable that affects professional work and behavior is the professional-client relationship. Research in professional-client relations has a long history in the sociology of professions literature, and has addressed a range of issues related to this relationship

(Rosengren, 1978; Kroeger, 1975; Greenlay & Schoenherr, 1981; Antle & Nalebuff, 1991; Fincham, 1999; Gendron, 2002). Up until recently, two features have characterized the dominant approach of studying professional-client relations. First, this relationship is studied as a dyad. This approach limits the study of variables (affecting the relationship) only to the client and the professional, neglecting other factors that may impact this relationship. Second, most studies focus more on the client, thus offering little understanding of how changes in the content and manner of service provision have impacted professional work and behavior. The weakness of this approach was especially evident during the Enron affair, where a range of professions and an impressive roster of prestigious professional service firms (PSFs) were found to be blameworthy. Extant research has consistently highlighted the importance of a positive reputation and high status affiliation, especially for professional service firms where the product is intangible, complex, and difficult to measure and price (Uzzi, 2004; Uzzi & Lancaster, 2006; Baker, Faulkner & Fisher, 1999; Jensen, 2006; Greenwood, Li & Deephouse, 2005). In light of this information, the actions of the professional service firms involved with Enron appear much more surprising. These prestigious PSFs, through their active involvement with their clients, ultimately put their own reputation, and potentially their survival, at risk.

The failure of Arthur Andresen and the subsequent investigations that plagued large professional service firms highlight the importance of understanding the dynamic in the relationship between large clients and large professional service firms. More importantly, it emphasizes the importance of exploring the consequences of such relationships for professional behavior. It is in this context that an emergent concept '*client capture*' becomes important. *Client capture* is term introduced by Leicht and Fennel (2001), who suggest that large clients, such as corporations, exercise substantial control and influence over professional work – its content, process, and delivery. Client capture is an interesting concept for two reasons. First, it highlights the role of the employing organization (i.e., the PSF) in influencing the nature of the relationship. Second, unlike the dominant approach of focusing on clients, client capture examines the consequences of the relationship for the professional. The next section introduces and discusses the concept of client capture in detail.

Client Capture and Professional Behavior

Client capture is a term used to characterize a specific set of professional-client relations that exist between large organizations and professional service firms. As it is, client relations with large organizations are different from the traditional sole professional – individual client model. Individual clients are rarely in a position to question the wisdom of professional advice, but large clients, owing to the availability of in-house expertise, have increasingly questioned professional practice resulting in a 'crisis of accountability' (Kevin & Leicht, 2001:104).

> "(More than ever) professionals of all kinds are asked to account for the expenses they bill for and incur. Lawyers must increasingly justify the fees they charge, and often face clients who will put out bids for legal services and hire firms from a price sensitive basis. Scientists must increasingly justify the cost effectiveness of their work amid a rising chorus of those who question the contributions of basic science to the betterment of the human condition…corporations have made considerable progress in reorganizing the delivery of numerous professional services to lower costs and increase accountability" (2001:105)

The increased influence and ability of a certain set of clients to 'undermine professional prerogatives and status' (2001:105) is termed as *'client capture'*. It alludes to ways in which the consumers of professional work (i.e., large clients) gain the ability to control the activities, timing and the cost of professional work. According to this concept, various factors contribute in clients gaining a dominant role in this relationship. Most large corporations have their own in-house professional departments with accountants and attorneys. There is enough expertise and knowledge within these organizations to influence the judgment and decision making of a PSF. The in-house concentration of expertise enables cost conscious corporate clients to shop for the services they consume. Both routine and non routine professional work is given to specialized practitioners who are increasingly dependent on one or few clients for specific types of business.

A more recent study examined the phenomenon of client capture in large accounting firms (Macy & Sale, 2003). The authors suggest "the internal corporate governance structure of the big accounting firm is fundamentally flawed" (2003:1167). They find that the incentive structure within accounting firms makes it virtually impossible for auditors to be independent of significant clients. "Often partners in big accounting firms have only one client. Their professional success depends on the quality of the relationship they form with the top managers of the client they are auditing" (2003:1168). The net result of this process is that the client can dictate what types of services they want and how much money they will pay for them. The long term professional relationship between clients and firms gets replaced by one stop shopping, where each complex transaction is farmed out to specialized firms. Furthermore, large corporations offer professionals in PSFs opportunities to work in new and exciting areas. Rapid internationalization has led to many PSFs following their clients to new markets. It increases the PSFs's ability to augment their range of service offerings and to have access to new markets. Finally, the formal and informal network of large organizations works as a strong referral conduit for PSFs. Not only does it enable them to reach other corporate clients, but it also enables them to cultivate and consolidate their own informal network in other arenas of social life. These changes are a far cry from the independent practitioner representing a particular professional system to clients who passively consume advice on how to best make their way through a system of specialized and esoteric knowledge.

Therefore, the concept of client capture becomes interesting for two reasons. First, it takes a contextual approach to exploring professional-client relations. For example, by focusing on incentive and compensation policies, promotion criteria, and governance mechanisms, it highlights how organizational forms influence the nature of professional-client relationships. Second, what is more significant is that client capture examines the consequences of this relationship for the professional. This approach helps in examining both the ways in which professionals are influenced by certain organizational forms to initiate and sustain client relationships, and how the relationship in turn affects professionals' ability to negotiate organizational and professional concerns.

As an emergent concept, the dynamics associated with client capture have neither been fully explored nor explained. For example, client capture does not account for factors such as reputation and embeddedness of relationships influencing the interaction between professional service firms and clients. Research on organizational tie dissolution suggests that a change in the client's resource needs – a change in the level of dependence for services and products provided by a supplier – can influence the risk of dissolution. In one study, the clients as well as the advertising agencies actively managed their dependencies. Corporate clients depended on advertising agencies for the creation of advertisements, information and access to advertising buyers, while clients reduced their dependence by using tactics as dropping, continuing, adding and switching agencies. Over time clients also allocated and reallocated their business in ways that compel agencies to provide better quality and additional services (Baker, Faulkner & Fisher, 1998).

Even with its current shortcomings, the concept of client capture offers an interesting avenue to examine professional-client relationships and relate it to professionals' behaviors. In light of the recent corporate scandals and the negative attention on the activities of prestigious PSFs, this concept enables us to ask an important question:

How do large prestigious PSFs get captured by their clients and with what consequence?

The question above guides this entire chapter. In the next and subsequent sections, I review the existing literature on professional-client relationships to discern the ways in which it elucidates the relationship that Enron shared with the large PSFs.

Historical Background

Early approaches to studying professions were devoted to the task of distinguishing professions from other occupations and to distil the essential qualities of professionalism. One of the most important features of professional practice, which is singled out in these accounts, is the service ethic. Members of professions are typically seen as motivated by altruism and a high respect for confidentiality in their dealings with clients. The service ideal emphasized that professionals provide service to whoever requests it, irrespective of client's

age, income, kinship, politics, sex, religion, and social status. It represented the ideal base on which relationship with clients can be seen to rest. In one of the central studies that addressed characteristics of professionals, Greenwood (1957) addressed professional-client relations in detail:

> "In a professional relationship, the professional dictates what is good or evil for the client, who has no choice but to accede to professional judgment. The client derives a sense of security from the professional's assumption of authority. The authoritative air of the professional is a principal source of the client's faith that the relationship he is about to enter contains the potentials for meeting his needs" (Greenwood, 1957:12)

Comforting as it appears, the notion of the client deriving 'faith' from professional interaction quickly had its share of detractors. Studies that followed (Freidson, 1960; Carlin, 1962; May, 1978) focused much more on the manner in which clients could influence individual professionals and their work. May (1978) suggests:

> "The reputation, the professional success or failure of the independent practitioner rests precisely with potential clients, who are precisely those not technically competent to judge. Thus the independence of the lone practitioner is somewhat illusory, for he is somewhat insulated from the competent judgment of peers and dependent on the good opinion of the laity." (May, 1978:12)

One of the earliest studies that focused on characteristics of professionals and clients is Harley and Grunberg (1962). They delineated three stereotypes of patients: the *hostile*, the *passive-dependent* and the *manipulative seductive*. They also derived three stereotypes of physicians: the *omnipotent*, the *anxious* and the *detached*. Combining the two sets of professional and client stereotypes, their study divided professional-client relationships into nine categories, which they suggest are 'found everywhere'. In creating a typology Harley and Grunberg (1962) acknowledged that their typology was an attempt to take a richer look at professional-client relationships:

> "References to the doctor-patient relationship usually carry the implication that it is as uniform and blissful as the curator turtle relationship at the zoo, and that it is invariably beneficial to the patient- so much so that he is grateful to pay the fee for service. We have been iconoclastic to indicate that it is a human relationship that varies with its components and which may or may not provide the medium through which modern medical science is brought to those who seek its benefits." (1962:206)

The Harley and Grunberg typology (1962) examined the health services and was not necessarily generalizable to all professional-client relationships. The theme of examining professional-client relationships grounded in their unique social context is carried further in two notable typologies: Johnson (1972) and Larson (1977).

Johnson's (1972) classification tapped into the phenomenon of increasing specialization within professions and related it to the 'specialist consumer' relationship (1972:43). He suggests that emergence of specialized occupational skills create relationships of social and economic dependence and paradoxically, relationships of social distance. Dependence upon the skills of others has the effect of reducing the common area of shared experience and knowledge, and increases social distance. The greater the social distance, the higher is the potential for autonomy. Social distance and autonomy create uncertainty that varies depending on the social structural context of the professional-client relationship. One of the variables that increased the degree of uncertainty is the esoteric character of the knowledge applied by the professional. The degree of uncertainty influenced the relative power of professionals with respect to clients, leading to three different kinds of control in professional-client relationships. (1) An occupation group with high levels of esoteric knowledge and a fragmented and heterogeneous source of demand can exercise power over its client. This situation was termed as *collegiate* control where the organized professionals dominated clients. (2) In situations where there is a single consumer (i.e., "a patron who has the power to define his own needs and the manner in which he expects those to be catered for" (1972:46)), the balance of power is more likely to favor the client, and is termed as *patronage*. (3) The final kind of control discussed by Johnson is *mediation* by a third party, such

as government or a health insurer that controls professional-client relationships or sets guidelines that affects them.

The other notable typology, Larson (1977), focused on a different aspect that influenced professional-client relationships – the increasing proportion of professionals working within bureaucratic organizations. This phenomenon had already led to studies that examined the impact of organizational features on specific aspects of professional work, such as the content, the process of delivery, and the degree of autonomy (Scott, 1965; Hall, 1968). But a key area of inquiry was examining the impact of bureaucratic employment settings on client service. Larson's study focused on the increasing trend of professionals working within organizations and the stage of development of the profession, to examine the different types of attitudes towards clients. According to her, "redefinition of the organization function and assertions of professional autonomy vis-à-vis the organizational hierarchy always touch upon the client orientation" (1977:188). She suggests that client orientation may take various forms. First, it may be *manipulative.* For example, in a marginal and recently emergent area of professionalization, professionals are likely to attempt to seek support among their clients for the professionalization efforts. Second, *indifference* to the client may be the norm in the case of a more established profession operating within large bureaucratic contexts. For example, doctors in bureaucratized health plans and large hospitals are more likely to be attentive to organizational goals than to their clients. Third, *hostility* towards the client may develop when the professional demands deference and compliance and enforces maximum social distance. It is more likely to manifest itself in cases where neither professionals nor clients have a role in choosing who to interact with. Fourth and finally, the isolating influence of the bureaucratic set up and the struggle to adhere to their professional ideals influences some professionals to adopt an attitude of *partisanship* towards the client. In doing so they may be supporting change oriented towards respecting and supporting clients.

The typologies and classifications discussed above are unique for a few reasons: first, they acknowledged and explored the changes that were impacting professional-client relationships. For example, Johnson's classification looked at the relative power asymmetry in different combination of clients and professionals: organized professionals and

unorganized clients; organized clients and unorganized professionals; and mediatories that may influence this relationship. Similarly, both Larson (1977) and Harley and Grunberg (1962) focused on changes experienced by a profession and how it may impact their attitude towards clients. Finally, both typologies (Johnson's and Larson's) were indicative of the trends which were to dominate the professional-client literature.

The range of issues that have been covered under the theme of professional-client relations has been quite diverse. It has varied from a focus on client characteristics and understanding sources of client satisfaction/dissatisfaction, to a focus on attitudes of professionals towards clients, to a focus on organizational features that impede client service, to studies on power asymmetry. Unlike the professionals and organizations literature, which has three distinctive streams, the professional-client literature does not show clear divisions. Nevertheless, two approaches tend to predominate much of this literature: the characteristics approach; and, the power asymmetry approach. Both these streams are concerned with client service and satisfaction. Both approaches also examine the changes in professional work that eventually impact clients; however, the central focus in each of the research streams differs slightly. The characteristics stream tends to limit its attention to client satisfaction. Here, studies focus on demographic characteristics, socioeconomic variables and organizational features to understand how changes in these variables impact client satisfaction. The power asymmetry stream is concerned with clients but concentrates more on the outcomes of the power difference that exist between professional-client dyads. Both of these streams are discussed in more detail in the following sections.

Research Streams

Professional, Client, and Organizational Characteristics: Research in this stream shows a temporal progression with the earlier studies focusing more on professional-client characteristics, likely building up on the available typologies. The later studies focus more on the features of the employing organizations to examine their effect on service provision and client satisfaction (Leeder, 1972; Sharma, 1999; Raynolds & Scott, 2000). Most of the work on professional-client characteristics can easily be grouped between the mid-forties to late seventies. This body of work focused on demographic characteristics, social indicators and

economic background to study this relationship (Kroeger, 1975; Goodsell, 1976; Greenlay & Schoenherr, 1981). For example, Hollingshed and Redlich (1958) examined the source of tension between professionals and clients. They found that tension can be caused by the differences in 'circumstances where the social background experiences of the practitioner and his clients are at such variance that this variance tends to influence both the effectiveness of the practitioner in performing the occupational expectations of his colleagues, and the compliance of the client in executing the wishes of the practitioner' (1958:112). Kadushin focused on 'the effect of social distance between client and professional on the stability of their interactions' (1962:517) Social distance is the diminishing of shared experience between professionals and clients that happens as occupational groups become more specialized. This study examined ministers, physicians and psychotherapists in their relation to their clients. It suggested that professionals who share 'thought ways' and 'day-by-day social intercourse' (which I connote as community), they are likely to be deemed closer to their clients. Specialist professionals such as MDs, with their technical expertise, create and perpetuate a divide between professionals and clients.

Research in law suggests that clients' demographic characteristics play an important role in the way lawyers treat them. Underprivileged and disadvantaged clients tend to get dominated by lawyers who impose their definition of the problem and solution on the client. Some studies also suggest that lawyers do not like interacting with assertive clients, yet by making demands on their time these clients were able to get better service (Hosticka, 1979). The general agreement within this body of work can be summed by Johnson and Martin: "What people are and what people do outside of the role specific to the client practitioner relationship profoundly affects what happens when people assume roles of clients and practitioners" (1962 : 212).

Gradually the focus of the studies shifted to organizations where professionals work, as these employment settings were considered to be an important variable in understanding client service and satisfaction. For example, Rosengren (1966) examines how hospital structures affect orientation towards clients. His study suggests that the greater the level of bureaucratization and specialization in hospitals, the more limited and circumscribed the care given to patients. Hospitals that were less bureaucratized and had lesser number of

professionals provided more 'encompassing' care to patients (1966:8). A similar example is Kruger (1995) who examines how client assistance from professionals varies across organizational forms. Some research especially in accounting suggests that the financial health of a client organization affects service provision (Antle & Nalebuff, 1991; Pratt & Stice, 1994). Others suggest that the compensation, reward and promotion criteria in PSFs influence the nature of clients they are willing to accept (Gendron, 2001). Studies in the area of health services and law have highlighted how professionals in government managed organizations tend to be more aware of organizational requirements and structure their client services in order to conform to the aims and goals of the organization. Within health services, some studies suggest that once professionals start working in government hospitals or health centers their attention to client needs tends to decrease (Brown & Swartz, 1989; Bailey, 2000). Other studies compare different organizational forms and the effect of organizational structures on client service (Greenlay & Schoerer, 1981).

The focus on organizational features and their role in influencing client service and satisfaction is a part of the body of research that examines the consequences of the shift from a traditional model of the lone professional interacting with clients, to professionals working in different organizational settings losing control over who to interact with. Whereas one part of that body of research examined the consequences of this shift for the professionals' autonomy and role conflict (Hall, 1968; Bucher & Stelling, 1969; McNair, 1991), the characteristics stream of research focused on the consequences for client service and satisfaction. Most studies that focus on features of the employing organizations share two general characteristics. First, they examine the impact of a professional's employing organization on client relationships and services. These studies acknowledge that specific features of employing organizations influence professional-client relations. The employing organization is seen as an important variable that redefines the service ethic (one of the core features of a profession) to fit with its own goals and objectives. However, similar to the research in professionals in organizations, the studies here focus on the impact of bureaucratic structures on client service provision and satisfaction. In sum, while the central approach in the characteristics stream has been to concentrate on client satisfaction, it has also helped in understanding variables that influence aspects of professional work. This stream of research provides interesting insights into the manner in which the differences in

demographic factors, socioeconomic variables, and skill levels influence the degree of shared experience and the level of autonomy claimed by an occupational group. The next stream of research has a different orientation. Similar to the characteristics stream, it continues to focus on clients but examines more the relative power difference between professional-client dyads and the resultant outcomes.

Power Asymmetry Approach: This stream of research tends to focus on the professional-client dyad, examine factors that make one of the partners more powerful, and explain the outcome based on the power difference. Early approaches to studying professions and professional-client relations focused primarily on the sole practitioner and their interaction with predominantly individual clients. This relationship allowed for professional accountability and highlighted the power of the client. A client had some control over a professional because he/she could affect the professional's ability to attract new clients (May, 1978). Sole practitioners depended on referrals from existing clients to get new ones. The increasing proportion of professionals in organizations fuelled an interest in exploring how power relations between professionals and clients have changed.

A search for articles that addressed power in professional-client relations can be separated into two groups. In the first and smaller group of studies, power asymmetry is studied more from the perspective of the unorganized clients, especially those dealing with professionals working in heteronomous professional organization. These organizations influence professionals to conform more to organizational aims and goals making client service secondary. Here, a professional's sense of achievement is derived more from a powerful employer and peers rather than from the public service ideal. Thus the power of clients to influence service access and delivery is greatly reduced. The power of organized professionals is explored in detail in Robinson (1978) in a study of government sponsored health care systems. Based on extensive interviews with clients, she classified client dissatisfaction in several categories: (a) *communication,* (b) *balance of power,* (c) *the professional personally,* (d) *adequacy of service* and (e) the *client's subjective feelings of discomfort.* Of all these categories the balance of power was the most important concern for the clients. It related to clients' perceptions of lacking a voice in the nature and process of service provision. Inequity of power, Robinson suggests, is caused by professional socialization, organizational concerns

and even social background differences. These forces encapsulate professionals in a different subjective world from the clients. Professions' stress on autonomy as a symbol of professional status contributed towards a sharp divide between how professionals view themselves and how they are viewed by their clients. Research within this group of studies highlights the gradual diminishing of client control because of the role of a key mediating variable – the employing organization. As clients interacting with professionals in bureaucratic organizations may not be able to choose the professional they want to work with, they lack the opportunity to build a consistent relationships resulting in professionals being more attentive to organizational goals and rewards. The transformative power of large bureaucratic organizations has been explored in detail within the Proletarianization literature.

The second and larger group of studies focuses on the power of organized clients, such as large bureaucratic corporations. This body of research suggests that the most effective challenges to professional authority, prerogatives, and compensation have come from large organized consumers such as corporations, which through their control of access to clients, and money to pay for professional services, have made considerable progress in reorganizing the delivery of numerous professional services to lower costs (Leicht & Fennel, 2001). But turning to the client for legitimation may occur in any profession. The client lends credibility to the activities of the professional and helps him establish his claims of value. To illustrate, Fisher (1969) discusses the increased role of the state in guiding scientific research through policy and funding decisions. His study observed that there was an ever increasing tendency for elite scientists in universities to become more and more dependent on the state for support of their work. Such a tendency encourages the producers of knowledge to forsake their role-model by formulating their proposals for research support in terms of the problems with which the state as a client is concerned, and in terms of finding practical solutions which rest on stable rather than transforming knowledge. Similarly Rex (1970) has argued that the institutionalization of science may be detrimental to innovation and scientific discovery for it tends to encourage what Merton (1957) has called the ritualist and to discourage the innovator.

Other examples from different disciplines also illustrate the power asymmetry approach. Research in accounting suggests that there are different factors that create power asymmetry.

Some studies point to the length of the relationship and client size (Louwers, 1998). Others look at the financial record of the firm (Knapp, 1985), suggesting that clients with better financial records have more influence on professionals than those with average or variable records. Some studies go beyond the inequity of looking at the dyad and look at factors such as nature of the issue being discussed. For example, Hackenbrack and Nelson (1996) suggest that if the level of engagement risk is low, the client is more likely to get their way. Lord (1992) suggests that in times of high competition clients are more likely to be more influential.

Both the characteristics and the power asymmetry streams have contributed to a better understanding of the professional-client relationship. The characteristics approach with its focus on individual professional-client dyads helped illuminate factors that affected the degree of shared experience and hence the extent of client satisfaction. As much as this approach was useful in studying individual professional-client dyads, it appears rather inadequate to explain the events at Enron. The focus on client satisfaction in the characteristics approach entails knowledge of all key variables influencing this relationship. In the case of individuals, demographic and socioeconomic variables provide a fairly reliable assessment of the social distance between the participants and therefore the extent of shared experience and satisfaction. The enumeration of comparable variables becomes difficult when the dyad constitutes large organizations. Individual level variables (which will still be important to some extent) are likely to be confounded with organizational level variables. However the crux of the characteristics approach – that variables that indicate the uniqueness of participants play an important role in professional-client relationships – is a lesson that can be used fruitfully when dealing with professional and client organizations.

The power inequity approach, at a preliminary glance appears more helpful in explaining the Enron situation. Based on the research in this stream, one would have to focus on a single event and posit that Enron being a powerful client ensured that the professional service firms did its bidding. However, this proves problematic too. First; research in this stream focuses on a single event or issue. Given that the relationship between large PSFs and their clients (such as Arthur Andersen, Vinson & Elkins and Enron) are built and sustained over a period of time, any understanding of this relationship is dependent on identifying every issue

and event negotiated through the term of this relationship. Second, given that the relationship between Enron and its associated professional service firms persisted for a long time, it ignores the possibility that clients and professionals may accommodate each other's interests in order to sustain the relationship. These weaknesses are discussed in more detail in the next section.

Weaknesses in the literature

Ignoring dynamics of professional-client relationship: One of the biggest weaknesses of the research on professionals and clients is its inertial and structured conceptualization. A characteristics based approach may give an impression that professional-client dyads with similar demographic and socioeconomic characteristics will have a higher probability of sharing a very cordial relationship. Limited attention is paid to understanding how decisions, interests and incentives are negotiated in this relationship. An absence of understanding the dynamics involved in professional-client relations hinders an appreciation of the uniqueness of this relationship. Not only do different professions have different norms of interacting with clients, this relationship is also structured to a large extent by the context in which it is situated. For example, as a fledgling organization, Enron needed credibility and status in the Houston business community, which it attempted to gain by offering higher than market remuneration to its external counsel and auditors (both of which were large and very prestigious PSFs). Later on, as Enron grew in size and prestige, one of the ways in which it influenced its external counsels and auditors was to offer them the option to shift to the client organization and handle the same work they did previously – only now for the client's advantage. In a study focusing on the interaction between managers and consultants, Sturdy (1997) suggests using a dialectical approach founded on reciprocal anxiety to study consultant-client relations. He suggests that consultants first provide a sense of reassurance to managers and at the same time try to create and reinforce insecurities. Accounting is another field that has started paying attention to the negotiations involved in resolving contentious issues related to financial statements (Gibbens, McCracken & Salterio, 2004; Beattie, Fearnley & Brandt, 2004). An attention to the dynamics involved in the professional-client relationships will help unravel how interests and incentives are negotiated and accommodated as an ongoing part of the relationship.

Focus on a single event: The second weakness of this literature is its tendency to focus on a single event or issue and take that as an indicator of the general nature of the relationship. This problem is exacerbated because most of the studies are quantitative or based on surveys. They tend to study one event and then generalize about the nature of the relationship based on the focal event. In accounting especially, most studies have explored professional-client relationships based on quantitative analysis of any one issue related to audits. This approach leads to two assumptions. First, it gives an impression that the way a focal event plays out is indicative of the general nature of the relationship. Second, inferring the general character of a professional-client relationship based on an event suggests that once structured, the relationship is fixed. The possibility that the relationship changes as it gets initiated, evolves and is sustained over a period of time is neglected. This weakness of ignoring the possibility of change in professional-client relations is again related to a lack of understanding of variables outside of the dyad. The interplay of the variables outside of the dyad is much more visible in cases such as Enron. During the Congressional hearing, the board of directors of Enron suggested that they did not take action against the management because the outside counsel and auditors kept them uninformed about the conflict of interest in the Special Purpose Entities (SPEs). Data from the Investor Research Responsibility Centre (IRRC) and directorship data from Board Analysts reveal an interesting phenomenon. Many of the directors on the Enron board were on other corporate boards which had Arthur Andersen as their auditor. From Arthur Andersen's perspective, its less than helpful attitude towards the client may cause some concerns with its other clients. At the same time, for the board, punishing a management that was outperforming market expectations would endanger their position and remuneration.

Ignoring the impact of the relationship on the professional: An interesting feature in the professional-client relationship literature is that it examines the manner in which the public service ideal gets affected because of the increased bureaucratization of professions or changing professional orientation. However, it studies the relationship only from the perspective of the client. The studies focus on client satisfaction, attitudes, perceptions of professionals and similar topics. Little research examines how changes in the content and delivery of services and the increasing notion of clients as 'co-producers of knowledge' (Greenwood & Lachman, 1996) affect professional work and behavior. Some recent qualitative studies have

addressed how training and socialization, compensation and incentive schemes and promotion criteria contribute in creating a client focused culture, thus relating professional development to employing organizations and client relationships (Dirsmith, Heian, & Covaleski, 1997; Anderson-Gough, Grey & Robson, 2000; Gendron, 2002). This area is still unexplored and warrants more examination.

The weaknesses highlighted above are common across research in different disciplines. Lack of attention to the dynamics of negotiation, and, generalization of professional-client relationships based on the study of a single event or issue holds true for studies dealing with professional-client relations in bureaucratic organizations and autonomous professional organizations such as law firms or accounting firms. Similarly most of the literature continues to neglect the impact of client relations on professional work and behavior. Recent studies in accounting (Cooper & Robson, 2004) highlight the need to go beyond simple explanations for accounting choices and examine more the role of corporate and industry history, structures of markets, social reputation and economic interests to understand how rules and standards are used. This is an important point which suggests that PSFs, in choosing certain interpretations, can define the nature of the client relationship. Furthermore, client relationships with the same PSF can vary, depending on among other things, the interpretation of rules/standards that the PSF chooses. This suggests yet another way of discerning the attitude towards clients – examining the manner in which professionals discuss work and responsibility. The ways in which client relationships are structured in turn affect professionals' abilities to negotiate client interests and professional concerns. In other words, the nature of professional-client relationship impacts professional behavior.

The dyadic manner of examining professional-client relationships may have been useful in the more traditional sole professional-individual client model but is inadequate in the case of the relationship that exists between large corporations that are clients for equally large PSFs. Here, a whole slew of additional variables such as status, relationships between members of the client and the professional organization, networks and the length of association start influencing the nature of the relationship. The above, along with such organization specific variables such as training, socialization, formal and informal processes of reward and compensation, are more likely to help us understand why prestigious PSFs get captured by their clients. Many of these variables, such as reputation, network, and expertise are

organization specific resources that can be leveraged and maneuvered in order to attain organizational goals and objectives. Therefore it is important to start examining this specific set of professional-client relationships (large client- large PSF) from a theoretical perspective that acknowledges the dependence that one has over the other, the unique resources that each possesses that play a role in determining the nature of this relationship, and that recognizes that organizations interacting with each other react to each other's actions. A theoretical perspective that fulfills these criteria is the resource dependency approach. Drawing most directly on exchange theory (Emerson, 1962), Pffefer and Salancik (1978) articulated the resource dependency theory in interorganizational relationships in which the relative dependence of organizations on each other is the critical determinant. The next section discusses the resource dependence approach and the insights it can provide in exploring the variables that influence client capture.

Resource Dependence Theory

Resource dependence theory, pioneered by Pfeffer and Salancik's (1978) work, takes its conceptual roots in Thompson's (1967) open systems view of organizations. It offers a compelling rationale for why firms form relationships with other organizations. The theory has two broad tenets: (1) organizations are constrained by and depend on other organizations that control critical resources for them and (2) organizations attempt to manage uncertainty and their dependencies upon external groups in order to acquire more autonomy and freedom (Oliver, 1991; Pfeffer & Salancik, 1978). In order to procure critical resources such as money, physical resources, capital and human resources from the external environment and reduce uncertainty in the flow of needed resources, organizations will try to restructure their dependencies with a variety of tactics. One of the most common tactics for reducing uncertainty is forming linkages with other organizations. Linkages are associated with many benefits. First, linkages reduce both vertical and horizontal external constraints through facilitating cooperation with regulatory agencies, customers, suppliers and competitors (Burt, 1980; Dooley, 1969; Pfeffer, 1972). Second, linkages enable the acquisition of information about the activities of the other organizations. Finally, linkages also lower transaction costs inherent with external exchange and ultimately improve survival

and performance (Hillman, 2005; Pfeffer, 1972; Thompson, 1967; Williamson, 1984). In particular, previous research has suggested that linkages between boards of directors enable firms to facilitate both resource exchange agreements and competitive confederations (Aldrich & Whetten 1981; Burt, 1980; Dooley, 1969; Pfeffer 1972).

Resource dependence resembles the power asymmetry literature in two key ways: (i) similar to the research on power asymmetry, studies in resource dependence tend to focus on dyads of interacting organizations; (ii) much of the research using the resource dependence approach tends to focus on outcomes of specific events based on difference in power, i.e., when the two organization's needs and dependencies on each other are not balanced, the net power in the relationship will accrue to the organization that is less dependent on the other, a problem shared by the power asymmetry approach. However, despite the similarities, there are key areas of differences between the power asymmetry and resource dependence approach. The first difference is simply in the level of analysis and consequently the range of variables considered in the resource dependence theory. As resource dependence tends to focus on available organizational resources, it addresses a much wider range of variables such as organization size, structural components (Boeker & Goodsterin, 1991; Greening & Grey 1992; Daily & Dalton, 1994), and board of director size and composition (Dalton, Daily, Johnson & Ellstrand, 1999; Westphal, 1999). Empirical studies in this area have focused on interorganizational relations such as corporate board interlocks (Lang & Lockart, 1990; Stearns & Mizruchi, 1993), introduction of new organizational initiatives as a result of institutional pressure and demand from key constituents (Ingram & Simons, 1995), and alliance between lobbyists and firms in order to influence government policies (Schuler, 1996; Schular, Rehbein & Kramer, 2002).

A more significant contribution of resource dependence theory is its articulation of strategies that organizations use to manage power relationships. This theory has been explicit in suggesting that managers make strategic choices within constraints (Hrebeniak & Joyce, 1985; Marcus, 1988; Pfeffer & Salancik, 1978) attempting to mitigate the influence of external pressures on their firms. Actors here do not have unbridled strategic choice but they do have some discretion over how to structure organizational relationships to manage the

uncertainties created by dependencies (Oliver, 1991). This exercise of discretion requires interpretation of demands and dependencies and appropriate adjustment of intra and interorganizational linkages. Thus in the face of external constraints, managers retain the ability to have some flexibility in the responses they make to manage their public image (Elsbach & Sutton, 1992) and to deal with organizational issues (Buccholz, Evans & Wagley, 1989; Gray, 1983; Marcus, 1988; Post, 1978; Sethi, 1979). In highlighting not only the bases on which resource dependence can lead to power, but also the means through which organizational actors can lessen their dependence, resource dependence theory highlights the importance of organizational size and resources in managing uncertainty. Very simply, large organizations have sufficient resources and scale that they can alter their contexts in a significant fashion (Pfeffer & Salancik, 1978). Thus large firms have more ability to develop administrative responses to environmental pressures than smaller firms.

In the context of the relationship between large clients and large PSFs the resource dependence approach offers opportunities for greater insights into understanding this specific set. First, a resource dependence approach enables the consideration of the unique resources being exchanged between the two organizations. From the PSFs perspective, one of the key resources is their expertise that is utilized by the client. For example, in the case of Enron, Arthur Andersen was not only one of the largest audit firms in the world, but was also an expert in the energy market, especially in oil and gas. This kind of unique resource would be attractive for a client such as Enron because it not only gave it access to specialized expertise, but also credibility. For Arthur Andersen, one way of ensuring its hold over the client would be to leverage its expertise during its interaction with Enron. But as Enron was a large and diversified client, one could argue that in order to get its own way it consistently exercised control over Arthur Andersen by regulating the level of access that the audit firm had in terms of providing additional services. However, even with a larger set of organization specific variables, the resource dependence approach does not provide an adequate explanation for client capture. Given the size of the PSFs involved with Enron and the number of clients each of them had access to, it should have been difficult for a single large client to exercise power on equally large PSFs repeatedly.

The professional-client relationships between large PSFs and their clients becomes much more complex because of the level of embeddedness created through repeated and prolonged interaction, which makes it difficult for either to exercise power on a consistent basis. Focusing on large law firms, Nelson (2005) suggests that these firms have considerable power because of the huge volume and variety of corporate and legal transactions they handle. Existing firms possessed established relationships with corporate clients (a considerable marketing advantage), and perhaps more important, the clients had already invested in the firm's acquisition of detailed knowledge in the business. Unless a new firm included lawyers who had previously done work for the client, either the client would need to pay start up costs once again or the law firm would have to absorb those costs. This creates a disincentive to switching for the client. Another problem with the current conception of 'client capture' is that it neglects to account for the importance of reputation. That is, it fails to account for the role of reputation as a buffer against client pressure. The significance of reputation as a source of competitive advantage is well acknowledged in research. Reputation becomes more central in the case of PSFs where the product is intangible and complex (Greenwood, Suddaby & McDougald, 2005). Moreover, a recent study suggests that performance of PSFs is related to their reputation (Greenwood, Li & Deephouse, 2005). In such cases, it seems reasonable to expect that PSFs will guard their reputation, which works both as a social cue for quality and a possible predictor of performance, zealously. Thus even with the additional insights from resource dependence theory, the current conception of client capture is still in consonance with the tradition of studying professional-client relationships as a dyad. It is unable to provide adequate explanation for an event such as Enron where a variety of professional organizations, such as investment banks, analysts firms, and law firms associated with the client were found to be blameworthy.

Therefore in order to understand situations such as Enron along with organization specific variables such as training and socialization, reward and compensation policies and approach to work and responsibility, other larger factors such as social networks, status and reputation become important in influencing the nature of the relationship. A more useful concept that

allows and accounts for the expression of these factors is 'organizational field'. The suitability of using organizational field in order to study client capture is discussed below.

The Field Approach to Client Capture

In the previous sections I highlighted the weaknesses of the literature on professional-client relationships, the relevance of resource dependence theory, and emphasized the need to focus on client-capture because of its unique professional-client dynamic. In this section, I advocate the study of this relationship using the concept of organizational field. I will first define the concept of organizational field and then explain how a field approach will enable the exploration of professional-client relations in a richer and more nuanced manner.

Organizational field is one of the key concepts in institutional theory. It has generally been understood as "those organizations that in the aggregate constitute a recognized area of institutional life: key suppliers, resource and product consumers, regulatory agencies and other organizations that produce similar services or products" (DiMaggio & Powell, 1983:143). Fields form when there is an increase in interaction among organizations and there is a development of mutual awareness among participants that they are involved in a common enterprise (Martin, 2003). Increased interaction among participants causes the emergence of sharply divided interorganizational structures of domination and patterns of coalition. This structuration of fields is largely a result of relations: relations that are both of direct interaction and of structural equivalence in ties (Podolny, 1994).

An alternative perspectives on fields emphasizes the ideational aspects of organizational fields (Scott, 1994); where they are viewed as product of patterns of mutual awareness, shared meaning systems and processes of structuration which are the natural result of organizational interaction (Suddaby, 2001). In this sense, fields are as much a methodological tool that helps discerning the boundaries the boundaries of mutual understanding and awareness between participants that compromise the field. The ideational perspective of fields is interesting because it helps in examining and enriching research that focuses on interorganizational relationships especially exploring the interpretive schemes underlying

different kinds of social networks. For example, in Enron's case, a quick read of the data indicated that there were a specific set of professional service firms that interacted with Enron over a period of time. Granted that professional-client relationships can be predominantly transactional in nature, but given the social nature of these transactions - the interactions through multiple channels, the frequent contact between professionals and clients - it is not surprising that such ties tend to persist over time. As research on social networks suggests ties become 'embedded' because they shape actors' expectations and opportunities in ways that differ from the logic of traditional expectations of professional behavior. "Embeddedness refers to the fact that exchanges within a group . . . have an ongoing social structure [that] , . . . by constraining the set of actions available to the individual actors and by changing the dispositions of those actors toward the actions they may take. . ." (Marsden 1981: 1210 in Uzzi, 1996). Thus, in this light the concept of a field helps in understanding the underpinnings of persistent set of social ties.

Recent work in resource dependence, stakeholder theory and networks has highlighted the importance of viewing exchange relationships formation and dissolution as affected by factors beyond the dyad involved. Jensen (2006) suggests that accountability induced status anxiety is an important factor in the dissolution of interfirm relationships. Status anxiety and therefore defections do not necessarily depend on the level of uncertainty surrounding firms but also depend on the audience to whom firms are accountable, how other firms have reacted to the events threatening their common partners, and their own commitment to quality. The results also provide strong support for the argument that firms are not only directly accountable to specific audiences but are also indirectly accountable for how other firms react to events, as other firms are used to make sense of ambiguous events and represent standards by which focal firms are compared.

A field approach is particularly pertinent for professional-client relationships for three reasons. First, it looks beyond the dyad of professional and client to acknowledge that other organizations interacting with them can affect this relationship. Second, a field approach allows for the expression of intangibles such as status and reputation in understanding the dynamics of professional-client relationships. Third, the concept of field provides a helpful

way of drawing boundaries around different sets of interacting organizations. In addition, it helps in examining the key events or behaviors that may indicate client capture. While unraveling processes of client capture, a field approach also highlights how interorganizational relationships influence professional behavior. Each of the above mentioned reasons for advocating a field approach is elaborated below.

The first advantage of a field approach is that it provides an opportunity to understand how professional-client relations get influenced by other organizations with which they interact. Recent studies in institutional theory have illustrated that PSFs borrow innovatory practices from similar organizations they have associated with (Sherer & Lee, 2002), which eventually affect their practice or the range of services they offer. A need to look beyond the dyadic approach is also advocated by the embeddedness literature (Granovetter, 1985; Uzzi, 1998; 2004), which argues that dyads do not provide a full picture of any relation because dyads are themselves embedded in larger networks of relationships. Any exchange between dyads has repercussions for the other members through transitivity (Uzzi, 1997). For example, when a client and auditor negotiate issues related to audits, the final product (i.e., the financial statement) affects other organizations (professionals and otherwise) interacting with both. Based on the information in the financial statements, investment banks, security analysts and members of the financial community make decisions about the attractiveness of the client. These decisions directly affect the reputation and viability of the client and may lead to restructuring of its relationship with the PSF.

The second advantage of grounding professional-client relationships within an organizational field is that it helps in highlighting the importance of status and reputation in understanding the processes in professional-client relationships (especially the relationships between large PSFs and their clients). Research on status suggests that organizations are more likely to partner with other organizations of similar status (Podolny, 1994). But status can be acquired indirectly by associating with partners of repute. For example, Enron as a fledgling firm needed initial credibility to be taken seriously. Enron chose to associate with Arthur Andersen, which was the most prestigious and sought after audit firm for energy and oil corporations. Enron was able to get the associational advantage of partnering with a reputable PSF. Later as the firm grew in stature and repute, it attracted the attention of larger

and more reputable PSFs like Vilson and Elkins (law firm), and Merrill Lynch (investment bank), and others.

This incident highlights two important issues. First, status and reputation play a very important role in shedding light on the motivation behind why some firms associate with certain partners. The need for credibility or to be seen as part of an elite circle can motivate client firms to target very reputable PSFs. In this way they get the associational advantage, which may then translate to increased attention from the market and other investors. Second, attention to status and reputation helps in understanding how interacting partners negotiate power shifts. As the above example illustrates, initially the client needed a reputable PSF to garner attention and credibility. Once the client grows to a point where it can offer similar advantages to other reputable exchange partners, the negotiating power of the client organization may grow manifold.

With respect to PSFs, reputation is the central resource that enables them to attract prestigious clients. Thus large corporations end up associating with large PSFs-accounting firms, law firms or investment banks. This network of elites, through repeated exchanges and working on projects together (accounting and law firms working together to structure deals), become committed to a shared sense of cohesiveness. An association of prestigious and reputable organizations ends up enhancing each participant's image. The benefits of this kind of association accrue to all (for the client, it may mean increased investment, for PSFs, more contact with other prestigious organizations and more projects). Thus the key dynamic in professional-client interaction is social relations. Cohesiveness is increased further when this group of organizations shares board memberships, informal relations and status affiliations.

The above discussion highlights the advantages of using a field-based approach to understand the motivation for PSFs and large client organizations to initiate and maintain relationships. The field approach also helps in grounding the network of relationships in its own unique context and sheds light on the manner in which the context shapes the nature of professional-client relationships. In order to understand the manner in which prestigious professional service firms got captured by Enron using resource dependence and

organizational field approach, two sets of variables become important. The first are organizational level variables that deal with the unique resources that professional and client organizations were able to leverage in order to accommodate each other's interests. The second are variables that address the nature of ties and the extent of embeddedness of professional and client organizations. For the organization level variables, professionals' accounts that address attitudes towards clients and their work and responsibility, instances of the use of policies and procedures within the organization that indicate client preference, and incentives and opportunities that were available for the client or the professional organization would provide an indication of the dynamic between professionals and clients. For variables that address reputation and status, accounts that address issues of client or professional issues, data about interorganizational ties, and the density of interaction will help in unraveling the process of client capture in the empirical chapter.

Chapter 6
Methods II

Introduction

Chapter Five provided an overview of the professional-client literature and also discussed the concept of client capture and professionals behaviour. One of the ideas highlighted in the chapter was the need to examine the relationship between large organizations and the professional service firms with which they work, using the concept of the organizational field. A field based approach allows for the expression of intangible factors such as reputation and history in the professional-client relationship. Another point emphasized in the chapter was the importance of examining professional-client relationships from the perspective of the professionals. It is in this context that the concept of client capture becomes interesting.

Client capture is a term originally introduced by Leicht and Fennel (2001) and used to characterize specifically the relationship between large professional service firms and client organizations. The term addresses the increased influence and ability of a certain set of clients to influence professional work and output. To recapitulate, professional-client relationships between large professional service firms and client organizations are different from individual professional-client dyads in two key ways. First, large clients have their own in-house accounting and law departments that harbor enough expertise and knowledge to be able to influence decision-making of professional service firms with which they work. Second, in-house expertise enables large clients to shop for specialized work which is eventually handled by partners in professional service firms who become dependent on specific clients. An alternate view suggests that because of the complexity and detailed knowledge acquired by the professional service firm regarding a client, client organizations too rely enormously on the professional service firms. This dependency is not an easy one to break as moving to new professional service firms entails time and effort in making the new PSF familiar with the client organization.

The availability of in-house expertise within the client and specialized expertise in professional service firms sets up professional-client relationships that are influenced by consideration of status, reputation and the history of previous interactions. Client capture offers the opportunity of understanding the dynamics of professional-client relationships between large organizations and professional service firms, and the consequences of this relationship for professionals.

This chapter focuses on the data and the analytic processes used to examine the relationship between Enron and the professional service firms it associated with. The first section discusses client capture in the context of the failure of Enron following which I present the qualitative and quantitative data used to examine professional-client relationships. The final section explains the analytic processes employed for both the quantitative and the qualitative data.

Client Capture and the Failure of Enron

The concept of client capture addresses the notion that large clients often posses enough expertise to influence the decision making of professional service firms with which they work. At a preliminary level the failure of Enron, the indictment of Arthur Andersen, and the subsequent investigations of the activities of reputable professional service firms tends to support the idea of client capture, i.e., the idea that large clients influence professional service firms to cater to their interests. However, even in the case of Enron such a characterization of the professional-client relationship leads to more problematic questions. First, even if Enron was able to influence its external auditor (Arthur Andersen), there were a host of other reputable professional service firms that were working with Enron who could have noticed the discrepancies in the financial statements. Why were other associated professional service firms not able to detect the discrepancies? Also, the professional service firms associating with Enron were very large firms having many clients. So why would they put their credibility at risk by enabling questionable choices of one of their clients? These questions emphasize the need to move beyond a dyadic consideration of the professional-client relationship to focus more on a set of stable interorganizational relationships that a client and professional service firms share, and to examine the influence of intangible

variables such as reputation and historical patterns of interaction that may influence the decision- making of professional service firms.

A network of relationships interacting on a regular basis is bound to have consequences for professionals' behaviour. Some of the results flowing from the network were highlighted during the Congressional Hearings. The complete *absence* behaviours such as taking the initiative to voice concerns, acting independently in cases of inaction by seniors, and internal whistle blowing were seen by Congressional Representatives as a deliberate act of professionals in professional service firms to marginalize the interests of the average investor by privileging the interests of their client. Additionally, there were other indications that professional service firms involved with Enron were endorsing Enron despite public information that questioned Enron's claims of financial well-being. To illustrate, even as Enron's stock price fell from U.S.$ 92 to U.S.$ 32 within a span of twelve days, and despite reports that senior Enron executives were selling huge amounts of their stock options, analysts associated with investment banks partnering with Enron continued to rate Enron as an 'investment grade' stock. In fact, the only sell recommendation that Enron received was from independent research firms that did not deal with any investment functions. The absence of 'professional' behaviours along with indicators such as the positive endorsement of a client whose financial health was questionable suggests that professional service firms either did not do due diligence regarding Enron, or colluded with Enron to make its financials appear better than they actually were.

The above discussion highlights the need to collect data on: (a) whether a network of stable relationships exists between some professional service firms and the client and (b) to explore the consequences of this network on professionals' behaviour.

Data

As the central argument in this chapter focuses on the importance of taking a field level view of the relationship between professionals and clients, I used two different types of data. The first type of data was quantitative and was used to indicate the field level relationships that existed between large professional service firms and their client. It was aggregated using

three different databases, *Board Analyst, I/B/E/S* and *SDC Platinum*. The second type of data is qualitative and comprises of the transcripts of the Congressional Hearings related to Enron where several professional service firms offered testimonies.

Quantitative Data

Field level interactions were examined in three ways. The first was by examining the organizational affiliation of the board of directors for Enron. Here, the intention was to find the indirect ways in which Arthur Andersen was connected to Enron. The second was to focus on new equity (capital-raising) issues which provide information about professional service firms involved in this process. The third was to examine the recommendation of analysts affiliated with investment banks partnering with Enron in the equity deals. In order to trace these interactions three databases were used:

a) *Board Analyst*: to explore the indirect ties between organizations that Enron's board of directors was affiliated with, and Arthur Andersen.
b) *I/B/E/S*: to gather information on analysts' organizational affiliation and their recommendation regarding Enron's new equity issues.
c) *SDC Platinum*: to get detailed information about the professional service firms involved with Enron's equity issues.

Each of the databases and the data collected from them is explained below.

Board Analyst: It is an extensive database that provides governance and compensation information. *Board Analyst* covers virtually all firms of the S&P 500 and Fortune 1000 along with other mid sized and small sized firms. The database contains information about corporate boards, directors, executive compensation, shareholder proposals, and more. I used this database to find Enron's Board of Directors, their tenure and organizational affiliation (apart from Enron) for the year 2000. For example, a typical entry for a director appears as shown below:

"Mr. Savage has served as Chairman of Alliance Capital Management International (a division of Alliance Capital Management L.P.) since 1995. He currently serves as a Director of Lockheed Martin Corporation, Enron Corporation, and Qualcomm Corp".

As the database contains aggregated data starting from the year 2000, data on the board of directors for earlier years was difficult to come by[1]. Then I went through the annual reports of the affiliate organizations to find their external auditor. One of the reasons for this step was triggered by the Congressional Hearings. Some of the directors of Enron who testified complained that even though Arthur Andersen knew of the problems with the different financial structures, they deliberately withheld the information from the Board. In exploring whether the Enron directors were on other organizational boards which had Arthur Andersen as auditor, I wanted to map the indirect ways in which this Big Five accounting firm was linked to Enron.

Another way to discern the strength of professional-client relationships is to focus on important client activities and map the interaction of firms that were involved in these activities. For my study I focused on new capital raising deals (equity issues) of Enron. For any large organization such as Enron, raising capital on a regular basis for new endeavours is an important event. It involves a slew of professionals - from the underwriters who help in raising the capital to the bookrunners who help in setting the price. It also involves auditors who certify the quality of the new issues as well as legal advisors. Underwriters are investment banks which act as an intermediary between the issuer of deals (i.e. Enron) and the investing public. Bookrunners are investment banks which are responsible for setting the prices of the new issues. Auditors vouch for the financial quality of the new issues while law firms are present as legal advisors.

Repeated interaction with a particular set of professional service firms in this area would indicate well established relationships. I focused on the capital raising deals for Enron from 1995-2001, and subsequently focused on a set of seven professional service firms.

- Salomon Smith Barney
- Credit Suisse First Boston
- Goldman Sachs & Co
- J. P. Morgan

[1] Although there are other databases that contain Enron's board of directors information for years prior to 2000, detailed biographical information and organizational affiliation as present in the Board Analyst is difficult to acquire.

- Merrill Lynch
- Arthur Andersen
- Vinson & Elkins

The above seven firms were chosen for two reasons. First, as I went through the database that contained information about Enron's equity issues, these seven firms appeared to have more interaction with Enron compared to other professional service firms. The second reason for focusing on these firms was that most of them participated in the Congressional hearing, thus providing the opportunity of examining their accounts of work and decision-making in greater detail. In case of the investment banks, several of them had analysts who were involved in issuing recommendations for Enron.

Two databases were used to aggregate information about the new equity issues and professional service firms that associated with Enron in these endeavours: *I/B/E/S* and *SDC Platinum*. The data related to the organizational affiliation of analysts and their recommendations of Enron's equity issues was aggregated using the *Institutional Brokers Estimate System* (I/B/E/S) which monitors the earnings estimate on certain firms. This database covers around 18,000 companies in 60 countries and contains data from more than 850 analyst firms. *I/B/E/S* is unique in that it uploads data on an analyst-by-analyst basis. The analysts and brokers are identified individually and independently, thus providing the opportunity to track an analyst across brokers. Using *I/B/E/S*, I went through analysts' organizational affiliations, chose the ones from Salomon Smith Barney, Credit Suisse First Boston, Goldman Sachs & Co, J. P. Morgan, and Merrill Lynch, and aggregated their recommendations regarding Enron new equity issues from 1995-2001. It is important to note that the credit rating scales used by analysts from different organizations varies substantially. For example, Salomon Smith Barney has a five point alpha numeric scale, while analysts at Royal Bank of Canada (RBC) Capital Markets used a three point alphabetic scale. Therefore it is difficult to compare the ratings of two analysts from two different firms. For example, Smith Barney Citigroup's highest rating is *'Outperform'* which is the same as Paine Webber's *'Attractive'*. In order to bring some level of comparability to these rating scales, *I/B/E/S* uses its own decoder to standardize ratings as *'strong buy'*, *'buy'*, *'hold'* and *'sell'*. For purposes of analysis, I used the *I/B/E/S* standardized ratings.

The new issues data was aggregated using the *SDC Platinum* database. This database contains information about SEC filings, equity, corporate debt, and taxable municipal debt that are underwritten in the United States. For equity (capital raising deals) issues, the database contains information about underwriters, bookrunners, law firms, auditors and trustees along with fees and expenses. However, there is one limitation to this database. Firms offering new equity issues (capital raising deals) are not required to file all of the information, so much of the information available is voluntary. In many cases with Enron, though I knew the total number of capital raising deals, I did not have complete information about the professional service firms participating in them.

The quantitative data would reveal the formal relationships between Enron and some of the professional service firms. It would help in understanding whether there existed a pattern and history of relationships between this large client firm and the professional service firms it associated with. Important as it is to establish that Enron shared a stable relationship with a set of professional service firms, it is more important to understand the *consequence* of a relationship of this nature for professionals in the professional service firms. The manner in which client relationships are perceived by professionals, and how they influence professionals' decision making will be explored using the qualitative data.

Qualitative Data: The qualitative source of data was the Congressional Hearing, which contained transcripts of the hearing involving the investment banks, analyst firms, Enron's external auditor, external counsel, and credit rating agencies. Within the hearings, Congressional Representatives were keen on understanding the nature of information that the professional service firms possessed and the basis of their decision making. Such issues afforded the opportunity to explore the professional-client relationship more from the perspective of the professionals. Issues related to the strengths and limitations of qualitative research, the use of archival data, and questions of *interpretive* and *theoretical* validity have already been discussed in detail in Chapter 4 and remain the same for the qualitative data utilized in this study.

The next part is divided into two sections. The first section deals with the analysis of the quantitative data and the second section discuses the analytic processes used for the qualitative data.

Analytic Procedures

In this section I discuss the processes used to analyze the quantitative and qualitative data. The quantitative data was used to examine field level interactions, i.e., to uncover whether there is a set of professional service firms that consistently interacted with each other. The qualitative data was analyzed separately and was used to examine professionals' perceptions of their relationship with Enron.

Part 1

I used two different indicators to look for professional service firms that consistently interacted with Enron. The first indicator was looking at the board of directors of Enron and their organizational affiliation. Much of the research on board interlocks suggests that interorganizational connections established by outside directors are very important for several reasons. First, they serve as a strong indicator of the reputation of a firm. Second, director interlocks are a powerful mechanism of communication that may influence strategy, structure and even performance of interlocked firms. Finally, interlocks are a reliable indicator of a firm's network (Mizruchi, 1996; Westphal & Zajac, 1995; Granovetter, 1985; Useem, 1979). It is then possible that professionals interacting with a large client view the board as a possible source of new client ties, and would concentrate on maintaining cordial relations with the directors. In order to explore this reasoning I extracted the list of the board of directors of Enron in the year 2000. *Board Analyst*, a database that aggregates director information, also provides all their organizational affiliations.

Once the information about the affiliate organizations was clear, I used the annual reports of the year 2000 which contained auditor information. Using the database and annual reports, I compiled Enron's board of director affiliations.

The second indicator of a stable set of professional service firms interacting with Enron was equity issues. Equity issues are new deals structured to raise capital. These appeared to be a good starting point because of the involvement of the number of professions in executing these deals successfully. As Enron was the sixth largest firm in the United States, the amount of capital it raised through new issues for expansion and other activities was very significant. Table 1 provides the total sum that Enron and the professional service firms raised each year from 1995 to 2001.

Table 6-1: Amount of Capital Raised by Enron and its Associated Professional Service Firms.

Year	$(Millions)
1995	$ 2,065.90
1996	$ 1,514.40
1997	$ 4,808.20
1998	$ 3,565.00
1999	$ 8,060.50
2000	$ 5,104.10
2001	$ 3,593.60

Table 6.1 indicates that the amount of capital raised through these equity deals would have made Enron an attractive client for many professional service firms. As mentioned earlier, the *SDC Platinum* database does not have complete information about all of the equity issues initiated by Enron, therefore the total amount of fees paid to firms associated with Enron is inferred through the available information. For example, in 1995, the investment banks were paid almost U.S. $1.05 million per deal. In 1995, Goldman Sachs earned U.S. $6.205 million as management fees; in 1999, Merrill Lynch earned U.S. $ 21.88 million. As Enron's external auditor and consultant Arthur Andersen's fees were substantial. To illustrate, in 2000 Enron paid Arthur Andersen U.S. $52 million for audit and consulting services, almost U.S. $1 million per week. Similarly, as external counsel, Vinson & Elkins LLP charged Enron U.S. $32 million in 2000.

On average Enron initiated fifteen deals per year with the maximum number of twenty three in 1999 and a minimum of eight in 1996. The data on *SDC Platinum* and on *I/B/E/S* is uploaded and updated on a daily basis which gives it richness but at the same time makes the data cumbersome to manage. Further, the data is presented in terms of new issue per year.

Every time Enron came out with a new equity issue, the information related to that issue (i.e., the amount, financial advisors, legal counsel, underwriters, and bookrunners) was uploaded as a separate event. In order to make the data more manageable and to get a pattern of relationships, I reorganized the available information based on four variables: underwriters (investment banks); bookrunners; auditors for new issues; and legal counsel. To illustrate, Table 6.2 shows the investment firms involved with Enron in the equity issues from 1995-2001.

Table 6-2: Investment Banks Involved with Enron's Capital-Raising Deals.

Year	Salomon, Smith Barney	Credit Suisse First Boston	Goldman Sachs & Co	JP Morgan	Merrill Lynch	Total Number of new Issues
1995	7	0	5	0	3	12
1996	2	0	2	3	1	8
1997	5	2	2	3	5	18
1998	1	4	2	1	5	14
1999	5	5	2	4	5	23
2000	4	4	0	1	3	16
2001	4	2	0	1	3	19

Similarly, the analyst data containing recommendation is uploaded on *I/B/E/S* based on each new equity issue. The data on *I/B/E/S* contains the original documentation as sent out by the firm. As analyst scales vary across different organizations, *I/B/E/S* has its own decoder which standardizes the recommendations from all firms. To illustrate, Table 6.3 shows a snapshot of the analyst recommendations for eight new Enron issues in 1995 along with the *I/B/E/S* decoded recommendation.

Table 6-3: Snapshot of Analyst Recommendation

Recommendation Date, SAS Format	Company Name	Broker ID	Bank Name	Broker Recommendation Code	Broker Text	IBES Recom
19950109	Enron Liquids	Mitch	Paine Webber Incorporated	3	Neutral	Hold
19950109	Enron Oil &Gas	Smith	Smith Barney Citigroup	2	Outperform	Buy
19950110	Enron Oil &Gas	Kemsec	Everen Securities	2	Market Performer	Hold

19950117	Enron Oil &Gas	Lehman	Lehman Brothers		Market Performer	Hold
19950123	Enron Oil &Gas	Mitch	Paine Webber Incorporated	2	Attractive	Buy
19950125	Enron Oil &Gas	Morgan	J P Morgan		Neutral	Hold
19950201	Enron Global	Smith	Smith Barney Citigroup	2	Outperform	Buy
19950214	Enron Global	Lehman	Lehman Brothers	1	Strong Buy	Strong Buy

As shown in Table 6.3, *I/B/E/S* data are originally organized by issue and individual analyst. Therefore, in order to look for the pattern of relationships, I reorganized the data on two different bases. First, I combined analysts' recommendations for new issues by year, and second, I noted the individual analysts' organizational affiliation by year.

Part 2

The analytic processes involving the qualitative data were similar to the ones discussed in Chapter 4. However, as this group of qualitative data had different orienting questions, the analysis led to a different set of issues and categories. The data was analyzed in four stages.

The orienting question directing the qualitative data focused on why, despite possessing knowledge and expertise, reputable professional service firms were caught unawares. Given the orienting question, I was more interested in understanding the perspective of the professionals (from the PSFs) who interacted with Enron. Therefore, I focused more on the Hearings that contained the testimonies from Arthur Andersen, Vinson & Elkins, Smith Barney (Citigroup), Morgan Stanley, Goldman Sachs, analysts affiliated with the investment banks and analysts from three credit rating agencies – Standard & Poors, Moody's, and Fitch.

In the first stage I collected textual extracts from all of the Hearings and reorganized them on the basis of employing organization. This step offered the opportunity to examine if professionals' perception of client relationship is shared by others in the same organization

Table 6.4 lists the testimonies used for examining the relationship Enron shared with the various professional service firms.

Table 6-4: Testimonies used for Professional-client Relationship

Organization	Testimonies	Position and Organization Affiliation
Accounting Firms	C.E. Andrews	Senior Executive, Andersen LLP
	Michael C. Odom,	Audit Partner, Andersen LLP
	Dorsey L. Baskin, Jr.,	Managing Director, Professional Standards Group, Andersen LLP
	Nancy Temple	Attorney, Andersen LLP
	Joseph F. Berardino	Managing Partner/CEO, Arthur Anderson, LLP
	Ellen Masterson	Partner, PricewaterhouseCoopers, Partner-in-Charge of Global Audit Methodology and Global Leader, Value Reporting
	Thomas H. Bauer	Partner, Andersen LLP
Analyst Firms	Charles L. Hill,	CFA, Director of Research, Thomson Financial/First Call
	Thomas A. Bowman	CFA President and CEO, The Association for Investment Management and Research
	Scott C. Cleland	Chairman and CEO, The Precursor Group
	James K. Glassman	Resident Fellow, American Enterprise Institute
	Gregg S Hymowitz	founding partner, Entrust Capital
	Marc E. Lackritz	President, Securities Industry Association
	David W. Tice,	Portfolio Manager, Prudent Bear Fund
	Howard M. Schilit	CPA, President and Founder, Center for Financial Research & Analysis
Credit Rating Agencies	Ronald M. Barone	Managing Director, Corporate and Government Ratings Group, Standard & Poor's
	John C. Diaz	Managing Director, Moody's Investors Service
	Ralph G. Pellecchia	Senior Director, Global Power Group, Fitch Ratings
Investment Bank and Analyst Firms	Charles O. Prince III	Chairman and Chief Executive Officer, Citigroup Global Corporate and Investment Bank
	David C. Bushnell,	Managing Director, Global Risk Management, Citigroup/ Salomon Smith Barney
	Richard Caplan	Managing Director and Co-Head, Credit Derivatives Group, Salomon Smith Barney North American Credit/Citigroup
	William T. Fox III	Managing Director, Global Power and Energy Group, Salomon Smith Barney, Citigroup
	Michael E. Patterson	Vice Chairman, J.P. Morgan Chase and Company
	Robert W. Traband	Vice President, J.P. Morgan Chase and Company
	Andrew T. Feldstein	Managing Director, Co-Head Structured Products and Derivatives Marketing, J.P. Morgan Chase and Company
	Anatol Feygin	Senior Analyst and Vice President, J.P. Morgan Securities
	Richard Gross	Analyst, Equity Research Division, Lehman Brothers
	Curt N. Launer	Managing Director, Global Utilities Research Group, Credit Suisse First Boston
Law Firms	Ronald T. Astin	Partner, Vinson & Elkins, L.L.P
	Joseph C. Dilg	Managing Partner, Vinson & Elkins, L.L.P

Separating the professional accounts on the basis on organizations generated a list of two accounting firms (Andersen, LLP and PricewaterhouseCoopers), one law firm (Vinson & Elkins, LLP), analysts from three credit rating agencies (Standard & Poor's, Moody's, and Fitch's), and bankers from five investment banks with analyst functions (Citigroup Salomon Smith Barney, Goldman Sachs, J.P. Morgan Chase, Lehman Brothers, and Credit Suisse First Boston).

The initial coding related to different aspects of professional-client relationships, professional output, and decision making. The analytic process was designed to be as exploratory and inductive as possible; therefore it was the data that finally directed the emergence of the main issues that influence professional-client relationships. The coding in the first stage was quite broad, focusing mostly on professional output and other topics such as the nature of contact between professionals and the client. The initial set of topics dealt with variable such as interaction, time, and fees, which related to aspects that may influence professional-client relationships. I also coded broadly for professional output such as financial structures, contracts, and reports that alluded to the consequence of professional-client interaction. As the coding proceeded, other topics emerged to be of interest, such as professionals' constant use of their employing organization's processes and procedures to build a rationale for the decisions they took.

In the second stage, the coding was more focused and refined. Here, the decisions behind the professional work emerged as a strong issue. One of the advantages of focusing on the decision-making and the rationale behind decisions was that it led to other issues common across professionals in all of the professional service firms. For example, accountants, analysts and investment bankers all addressed what they perceived as professionalism and responsibility. Most of them referred frequently to aspects of their employing organizations and the nature of the contacts between them and their client. The presence of all of these issues made comparison across different professional service firms possible. Focusing on professional output would not have provided the same kind of opportunity for comparison. The nature of contact remained an important issue but was split into (a) frequency of contact and (b) history of interaction. History of interaction included textual extracts where

professionals mentioned their association with the client to explain why they participated in certain projects.

There were two unanticipated issues, reputation and reciprocity, which turned out to be quite important and surprising. Reputation was an issue that professionals used on a consistent basis to explain their action. What surprised me was the role that reputation played in professional choices. Many of the professionals ignored the due diligence behind Enron's projects because of the reputation of the other professional service firms involved. When asked if they do the same for all their clients, these professionals emphatically denied that they would do so. For example, investment banks generally request that their own financial advisors and legal counsels look over their client's deals, but in the case of Enron they did not do so because they assumed that, if the accounting was deemed appropriate by Arthur Andersen, it must be so. Vinson & Elkins, who were supposed to investigate the concerns expressed by some professionals in Enron decided not to pursue those concerns in full measure because it involved a Big Five accounting firm. Finally, based on my reading of the Congressional Hearing transcripts, I found eight issues that emerged as important and significant. These are described in Table 6.5 below:

Table 6-5: Major Issues Emerging after the First Step of Analysis

	Issues	Definitions
1	Decisions made on the basis of publicly available information	These were a set of textual extracts containing the explanations of decisions taken by professionals based primarily the publicly available information about the client
2	Decisions made on the basis of informal information	The set of textual extracts which containing explanations of professionals that used information that was available only through informal means.
3	Contact	This set of extracts enumerated the extent of contact that existed between professionals in professional service firms and Enron.
4	History of Interaction	This denoted references of the length or history of interaction
5	Reputation	These extracts addressed professionals' perceptions of the status of other professional service firms involved in the relationship with Enron and the client organization itself
6	Reciprocity	This set of textual extracts referred to the acts of mutual benefits between professional service firms and clients
7	Structure of professional service firms	Here the set of textual abstracts referred to the different aspects of formal structures such as separation of divisions, roles and responsibilities within professional service firms

8	Model of Professionalism	Textual extracts that allude to conceptions of professional responsibility

Table 6.6 shows the total number of textual extracts found in each of the eight issues

Table 6-6: Number of Textual Extracts Related to Each of the Eight Issues

	Decisions made on the basis of publicly available information	Decisions made on the basis of informal information	Contact	History of interaction	Reputation	Reciprocity	Structure of professional service firms	Model of professionalism
Number	75	124	33	26	115	57	138	79

Table 6.6 shows that there is a significant difference between the numbers of textual extracts across different issues. One of the reasons for this difference is the variation in the number of professionals testifying from each organization's type. For example, there were more investment banks than accounting firms that testified, leading to many more professionals from the banks discussing their work. The least number of participating professionals were from the law firms. In fact only Enron's external counsel, Vinson & Elkins, LLP, participated in the Congressional Hearings. Within the accounting firms, professionals from Arthur Andersen, and a partner from PricewaterhouseCoopers, were forthcoming with their accounts. The professional group most forthcoming was the analysts. Table 6.7 provides illustrative extracts of the eight major issues that emerged from the second stage of analysis.

During the hearings, professionals were first given the opportunity to discuss their work in a statement which was made part of the Congressional proceedings, after which the Representatives asked questions about specific aspects of professional output and decision-making. Table 6.7 provides some example of textual extracts that illustrate the eight major issues.

Table 6-7: Textual extracts that illustrate the major issues

Decisions made on the basis of publicly available information	**Mr. Ronald Barone (Managing Director and Analyst, Standard & Poor's):** I am Ronald M. Barone, a Managing Director in the Corporate and Government Ratings Group of Standard & Poor's. One of my roles was to serve as an analyst and then a manager with respect to our ratings work for Enron. On behalf of Standard & Poor's, I welcome this opportunity to appear at this hearing. As a member of the financial community that relied on Enron for complete, timely, and reliable information, and instead received incomplete, deceptive, and, it now appears, fraudulent representations, Standard & Poor's supports the Committee's urgent sense of the need to investigate the circumstances relating to Enron's collapse. At their core, our ratings opinions are based on the issuer's public information, including audited financial statements. We also may have access to certain confidential information-we did with Enron-but only to the extent the company is willing to provide such information. We expressly rely on the companies we rate not only for current and timely information at the time of the initial rating but for material updates to that information.
Decisions made on the basis of informal information	Moody's person: Our strong record is due in large part to the availability of reliable information. The combination of the financial disclosure regime in the United States, audited accounts, information that is provided directly to Moody's, and issuers' good-faith dealings have normally been sufficient. As we have come to learn, Enron's public disclosures and its responses to our specific requests for information were misleading and incomplete. **Mr. Pellecchia (Analyst, Fitch Ratings):** The short answer, Mr. Chairman, is that we now know that we were not provided with accurate and complete information. A company's public certified financial statements are the bedrock of any analysis of the value or the prospects of a company's stock. It is now common knowledge that Enron's financial statements, which had been certified by its independent auditor, did not represent the company's true financial condition. **Representative Lieberman:** This was at the end of October, and that they had a special committee investigating? **Mr. Barone (Analyst, Standard & Poor's):** That's correct. **Representative Lieberman:** But, still, you felt confident enough to make the statement you did on November 2? **Mr. Barone (Analyst, Standard & Poor's):** That is correct. They explained to us that in the investigation: (1) they found, I believe, the LJM1, LJM2, Chewco, and Raptors; (2) they had started to scrub down everything they could get their hands on; and (3) they would be surprised if they would find anything further. And while they said clearly that they did not have the full report, they believed they had uncovered the majority of what there was to uncover, and that this was what they expected. **Mr. Fox:** Senator, this transaction was an interim bridge financing that we were engaged in. Our firm typically does not engage in bridge financings unless we are involved in the take-out or providing the permanent financing. In this case, we were not. So for this reason, I went and visited with Mr. Fastow because he had control of the take-out of this transaction. He was working with another institution. So we wanted comfort from him that they were going to take all steps necessary in order to ensure that the takeout financing was accomplished and our entire transaction would be repaid within its terms. **Representative Levin:** So he gave you this assurance that your so-called investment would be repaid within that 6-month period? **Mr. Fox:** He gave me the assurance that he would take all steps necessary to make certain that the take-out financing was accomplished and, therefore, the entire

Bacchus transaction would be repaid.
Representative Levin: Now, would you have reassessed your participation in the deal had you not obtained that support?
Mr. Fox: I believe we would have. That assurance was important to us. As I said, we were not involved in the take-out of the financing of Bacchus, and typically our firm would not be involved in a bridge financing that was dependent upon a take-out unless we were involved in the take-out, and we were not in this case.

Representative Levin: And then you later said the following. "The risk management has not approved this transaction for the following reasons," and then one of your reasons, which is the one, two, three, fourth bullet, is that "the GAAP accounting is aggressive and a franchise risk to us if there is publicity, a la Xerox." This transaction was a franchise risk to Citibank if there was publicity, that is what you said in this document. Were you telling the truth?
Mr. Bushnell: Yes, Senator.
Representative Levin: And yet, you went ahead with this. This is what really is so troubling to me from Mr. Prince's testimony and otherwise and why the explanation that we have heard this morning is so unsatisfying.

Mr. Barone (Standard & Poor's): Thank you, Senator. The confidence we had was gained from discussions with Enron's management at that time, the new president, Greg Whalley, and CFO Jeff McMahon. They explained to us that, as much as they knew, from their investigation, there were no further partnerships that had debt obligations that they were unaware of. But that, indeed, and as my comments stated, they had not fully completed all that the investigation was to provide.

Contact

Mr. Diaz: No. We had talked to Enron a few days before that and they had given us a heads-up on the writedowns that were to come and began to explain to us the equity charge. And we were very surprised at not only the asset writedowns they were taking but also at the nature of the equity charge. And we were questioning and scratching our heads about the type of accounting that they were using for that charge and how did that $1.2 billion of equity actually come about. They made a rough attempt to explain to us the complexity of the hedges, but we were not satisfied with their explanations.

Mr. Barone(Standard & Poor's): Yes, generally going back to your question, Senator, we were calling Enron, and--
Representative Lieberman: They were not initiating calls with you by and large?
Mr. Barone (Standard & Poor's): There was an active dialogue back and forth, Senator, as we do with many issuers. If they have news to tell us, they would be active and do that, or respond to questions. They would research our questions and they'd call us back with answers.

Mr. Pellecchia (Analyst, Fitch Ratings): Thank you, Mr. Chairman and Members of the Committee. My name is Ralph Pellecchia, and I am a Senior Director in the Global Power Group of Fitch Ratings. I joined Fitch in July 1989 as an analyst in the natural gas and power sector. I have been the lead analyst following Enron at Fitch since May 1997.

History of Interaction

Mr. Ronald Barone (Standard & Poor's): I am Ronald M. Barone, a Managing Director in the Corporate and Government Ratings Group of Standard & Poor's. From 1994 until Enron's bankruptcy in December 2001, one of my roles was to serve as an analyst and then a manager with respect to our ratings work for Enron.

Mr. Niles (Analyst, Salomon Smith Barney): Thank you, Mr. Chairman and Members of the Committee. Since March 2000, I have been the senior analyst at

Salomon Smith Barney for the integrated power and natural gas sector. Before that, and since 1997, I was the senior analyst for the integrated power and natural gas sector at Schroder. I covered Enron at both Schroder and at Salomon Smith Barney.

Representative DeGette: So you are aware in August an employee had made these allegations, and then Vinson & Elkins had done an investigation also in August; is that right?

Ms. Temple (Arthur Andersen): Not exactly. Before October 12, I was aware that Vinson & Elkins had been engaged and completed and reported orally to the board that the results of their investigation were positive. And the engagement team also assured the practice directors who were being consulted at that time and myself that they had reviewed the information about the allegations, and that the allegations were, to the extent that they had any information in them in reference to transactions, involved transactions that the audit team had carefully reviewed in its prior work.

Representative DeGette: So you thought that because Vinson & Elkins had said there was no problem, that that did not trigger any kind of requirement; is that correct? Yes or no, please.

Ms. Temple (Arthur Andersen): ... I noted that the law firm reported that there was nothing further to follow up on at that point in time; and this was a very large law firm was representing Enron Corporation.

Reputation

Representative Stupak: Not even by an accounting firm outside of Arthur Anderson?

Mr. Dilg (Partner, Vinson & Elkins): Arthur Anderson, again, was one of the Big Five accounting firms that had been chosen by the Audit Committee at Enron.

Representative Stupak: Right. And you never talked to any of those people.

Mr. Dilg (Partner, Vinson & Elkins): We talked to the leading engagement partner for Arthur Anderson.

Representative Stupak: Head guy at Anderson. Those people had substantial professional and personal stakes in the matter under review as it says in the Powers Report, right? Those were the people that were talked to.

Mr. Dilg (Partner, Vinson & Elkins): I don't know how they characterized the personal stakes they had in it. They had the credibility of their veracity on the line.

Representative Stupak: They had a dog in the fight, let's put it like that.

Mr. Prince (Citibank): First, though, let me say a few words about the specific transactions under review. While I believe our people acted in good faith, I think it is fair to say that we never anticipated that a financial intermediary like Citigroup would be criticized for the accuracy of the accounting treatment that a Fortune 10 company gave to its transactions with the express approval of a then-highly respected Big Five accounting firm. At the time we entered into these transactions, we never imagined that Arthur Andersen wouldn't even exist a year later or that a failure of ethics would have destroyed Enron, a company ranked in the top 20 on the list of most admired companies in the year 2001.

Mr. Diaz: Senator, I think I've testified before that we also believed that the probability of the merger going through was high. We had a rating committee that included our senior management, and we came to the conclusion, given the changes in that agreement, there was a very high probability the merger would go through. So that's the key for holding the rating during that period...the other point is that when things are going-when a company is under certain amount of distress, they would like for us to give the company the ability, if there's a probability of correcting the problem, to give them the opportunity to do so.

Reciprocity

Representative Greenwood: But did you ask Mr. McMahon for the names of these individuals that he complained about to begin with, in the first interview?

Mr. Dilg (Partner, Vinson & Elkins): I can't recall that we did.

Representative Greenwood: Didn't that raise any red flags with you that would cause you-I mean, I am trying to understand why the first thing you wouldn't have done, the next thing you would have done was say, "Oh, my God," pick up the phone, call these bankers, and say, "I am supposed to protect this company from liability, and there is a lot of liability that could result from these allegations if these allegations are true." I don't understand why you didn't feel a responsibility to Enron and stockholders to make those calls right away and find out what was really happening, not just taking Andy Fastow's word for it.

Mr. Dilg (Partner, Vinson & Elkins): You have to understand, Mr. Chairman, that in the context that the preliminary review was conducted, Mr. Skilling had just resigned from the company. There was a great deal of speculation in the market and with Enron's counter parties as to the reasons for Mr. Skilling's resignation. We were trying to develop the facts that we could by talking with people inside the company so as not to create lots of speculation and rumors until we knew what we could report to Mr. Derrick.

Representative Levin: Mr. Fox, let me ask you these questions. You are the one who met with Mr. Fastow to obtain this comfort for your bank. At our staff interview, you indicated that Mr. Fastow said that Enron would take whatever steps were necessary to make certain that Citibank's equity interest in Bacchus would be bought out. This was an important transaction for Enron, according to that same Exhibit 322(c). On the second page, this transaction was said to be "mission critical" by them and "a must" for Enron, and the words that I have quoted were on page one of that Exhibit 322(c) when it was said that Enron has offered to have the CFO discuss this "at whatever level of our organization we think necessary to obtain the right comfort." That is comfort now for Citibank. You knew that Enron was going to book this transaction as a sale, is that not correct?

Mr. Fox: That is correct.

Representative Levin: And you also knew that if Citibank did not truly have a 3 percent equity at risk, that it would be improper for Enron to book the transaction as a sale?

Mr. Fox: We understood that we had to be at risk for the 3 percent of the transaction.

Representative Levin: Well, it seems clear to me, Mr. Fox, that Citibank was aware that 3 percent had to be at risk. You just said so. You had to be assured that it would not be guaranteed in order for this to be booked as a sale. But to protect Citibank from loss, you went out and got a verbal assurance, a commitment, a statement that all steps necessary would be taken by Enron to pay you back. It was characterized properly by your assistant as a verbal guarantee. Did you receive an opinion that this was not legally enforceable?

Mr. Fox: We did not receive an opinion with respect to this aspect of the transaction. As I said earlier, my view was I was there. What I got was assurances from Mr. Fastow that the take-out financing would be executed, and we would be paid out of the entire transaction within its terms.

Mr. Launer: The only comment I would make is it is not our job to disclose material non-public information. It is the responsibility of the company, meaning Enron, their accountants and their lawyers.

Representative Levin: Why is it not the responsibility of your company, on the investment side of your company, to make sure that something which should be disclosed in that financial statement which would have an effect on the stock be disclosed?

Structure of professional service firms

Mr. Launer: Material non-public information. We are not over the Chinese wall and do not have possession of that information.

Representative Levin: By not insisting that it be disclosed, it is leading the other side of the company to be giving an appraisal of stock, a valuation of stock which is

based on information which the other side of the company knows to be incomplete. And it seems to me that creates an inherent conflict that we have to address and the investment community has to address.

Representative Tauzin: Does it have to be raised, Ms. Temple, when you are the counsel representing this company internally on litigation? Does anybody have to raise it, or is it somebody's responsibility in the company to say, stop destroying documents, we're under investigation? Whose responsibility was it if it was not yours? Did somebody have to raise it? Whose responsibility, Mr. Andrews? Was it the president? Was it you? Who was it?
Mr. Andrews (Partner, Arthur Andrews): In our policy, that responsibility-the policy that we're revising, and I acknowledge we're revising-in that policy, that responsibility is with the engagement party.
Representative Tauzin: With an accountant, not a lawyer? You give the responsibility to an accountant to decide whether it's legally permissible to destroy documents relative to a proceeding?

Representative Levin: What is the understanding that you have with your clients as to what is disclosed? Do you have a written agreement with them, a contract as to the amount of disclosure and what your access will be, inside access that is not publicly disclosed? Is that all set forth in a contract, Mr. Barone?
Mr. Barone: We have an agreement-I don't know if it's contractual or not, but it's an agreement that is included in our rating letter, that they provide us full, timely, and accurate disclosure of all material information relating to their rating. I don't know the exact words, sir, but it is quite broad and comprehensive.
Representative Levin: And they sign that, they agree to that?
Mr. Barone: Yes.
Representative Levin: Is that true with the other companies, too?
Mr. Pellecchia: We have a similar representation, but it's not a signed agreement.
Mr. Barone: Senator, I don't know-excuse me, I apologize. I'm not exactly sure they're signed or not. I don't want to represent--
Representative Levin: All right. Mr. Diaz.
Mr. Diaz: We have applications for ratings in which the maintenance of the rating is based on our satisfaction with the information that's being provided, but there's no specific agreement about the kind of or the type of information that has to be given to us.

Mr. Berardino: That is a very complicated question and a very fundamental question, Mr. Chairman. As you probably know, Enron was an extremely complex company. They had over 20,000 employees. In fact, I recently found out they had 600 CPAs. So they spent a lot of time trying to keep their books. They had 3,000 subsidiaries all over the world.
And as auditors, you know, we do not live there. We do test checks, we do statistical samples to inspect the transactions as the company presents us the information. And the company does have a legal obligation to present us information that we require. And ultimately our obligation was to ensure that the financial statements adhered to GAAP.

Model of professionalism

My point is that the rational, calm voice in the midst of turmoil should be the analyst.
Mr. Hymnowitz: Mr. Chairman, could I just comment on that last thing.
I actually respectfully disagree with you that we weren't warned or that analysts didn't do their jobs properly. Any investor should have just picked up the prospectus and read it, and all you had to do is look at the financial statements of these companies, and you would have seen the warnings.

Representative Stearns: In your testimony, you define the role of legal counsel.

Let me just read from this. "If a transaction", you say, "is not illegal and has been approved by the appropriate levels of a corporate management, lawyers, whether corporate counsel or with an outside firm, may appropriately provide the requisite legal advice."
So if a transaction is not illegal, not illegal and it's been approved by the corporate management, who determines whether a transaction is legal or not? Isn't that your job?
Mr. Dilg (Partner, Vinson & Elkins): Based on the information we would have at the time we were rendering the legal services, that's certain advice that we would give.
Representative Stearns: That kind of answer gets me concerned. If I understand, the whole purpose of V & E is to take the facts that are given to you, figure out if there is a legally appropriate way to do it, isn't that what your law firm does? Anderson comes to you, we want to do this, you show them how to do it legally. Is that the whole purpose of your law firm?
Mr. Dilg (Partner, Vinson & Elkins): That is the type of advice we render on certain matters, when we're asked. We do litigation matters. We do lots of different things.

Mr. Traband (Vice President, J.P. Morgan Chase): Thank you, Mr. Chairman. My name is Robert Traband and I am currently a Vice President of J.P. Morgan Chase Bank. Let me say at the outset, Mr. Chairman, that while we believe that our participation in the Fishtail and Flagstaff transactions was perfectly legal and followed established rules had we known then. What we know now about Enron's practices, we would not have engaged in these transactions with Enron.

Stage three of the analysis involved discerning higher level categories from the available issues. Three higher level categories evolved from the eight issues identified above: *nature of decisions, ease of access,* and *PSF ethos.* Each of these higher level categories is explained in detail below.

Nature of decisions: On reading all the textual extracts associated with the eight issues again led to a several key points. First, the decisions based on publicly available information and informal information showed two different characteristics. The decisions that used publicly available information were akin to '*statements of defense*', wherein professionals in the professional service firms played down their relationship with Enron and emphasized that their professional output was based only on the information that was available publicly to all investors. Therefore, it was the Enron executives that deliberately gave them fraudulent information for which the professional service firms cannot be held responsible. I labeled the second set of decisions as '*decisions of assent*'. These were a much larger set of textual extracts which indicated that professionals actually made decisions to participate, approve, and agree with financial structures, accounting choices and loan arrangements based mostly on the informal information that they had access to.

Ease of Access: The second major point was the discerning of key categories. For example, textual extracts related to *contact* and *history of interaction* indicated the *ease of access*, i.e., the effortlessness with which professionals were able to access time and contact with top Enron executives. *Ease of access* directed attention to the manner in which some of the professional service firms were able to use their past history to gain additional or more in-depth information compared to professionals from other firms who did not share the same history or have regular contact with Enron.

PSF ethos: This category refers to the combination of textual abstracts that address PSF structure such as professionals' reference to organizational divisions, roles within the organization, and organizational policies, processes and models of professionalism. It also refers to professionals' perception of their own responsibility. The reason for combining the two issues was that together they gave a richer sense of the manner in which professional work, and organizations where professionals work, interact with and influence each other.

A visual presentation of the relationships between the issues and higher level categories is presented in Figure 6A.

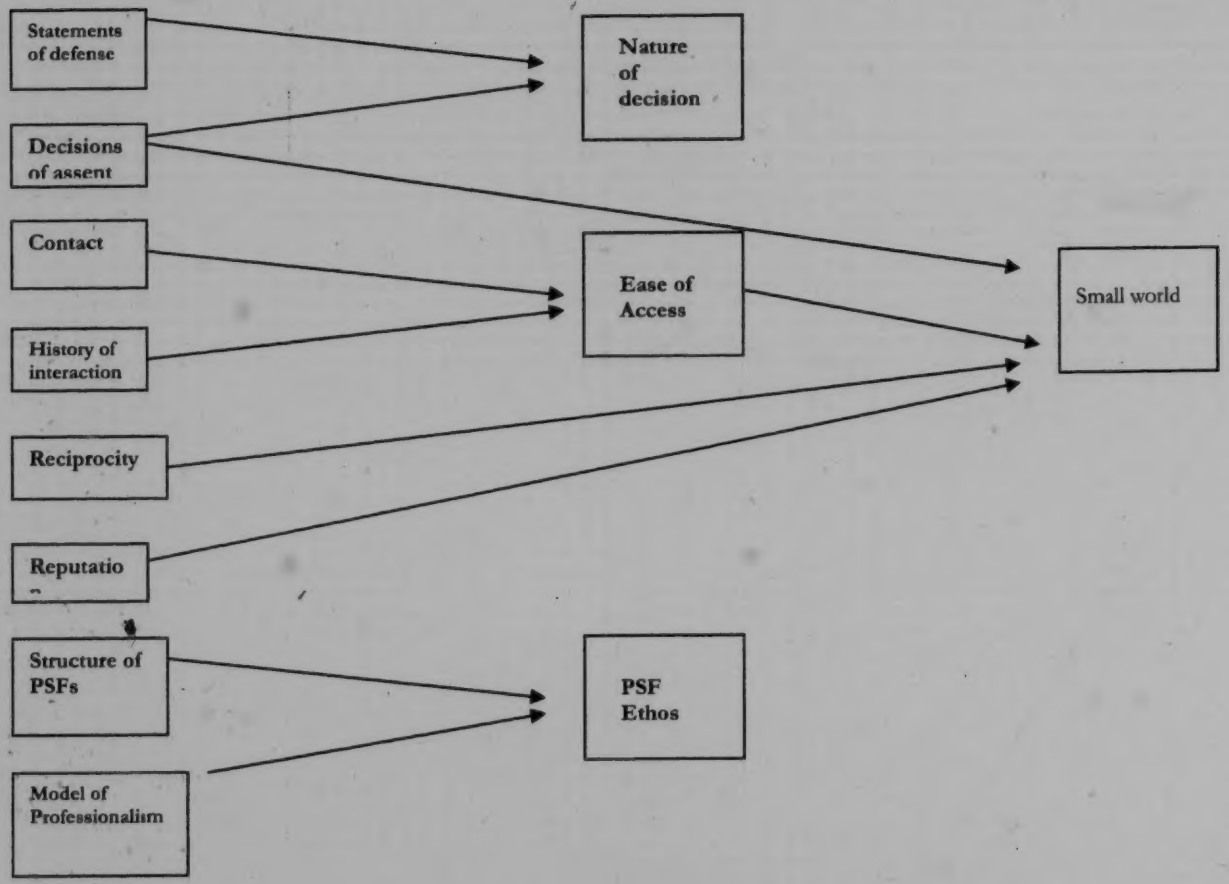

Figure 6A
Stage 3 of the Analysis: Deriving Higher Level Categories

The fourth and final stage of the analysis focused on examining how these higher level categories related to each other to help understand the variables that influence professional-client dynamics. In this stage, the textual extracts separated by the higher level categories (*ease of access, PSF ethos,* and *nature of decisions*) were rearranged with *reputation* and *reciprocity* to create a coherent narrative that dealt with professionals' rationales for their decision-making and of the role that client relationship played in the process. It was during this process of creating a narrative that *nature of decisions* appeared as the major explanatory category that could viably work as a proxy variable for ultimately understanding why a set of reputable professional service firms continued to support and endorse Enron in spite of the information they possessed. Within the *nature of decision*, *decisions of assent* related most strongly to professionals' perception of their relationship with the client and eventual behaviour. *Decisions of assent* combined with *ease of access, reciprocity* and *reputation* led to the emergence of a still higher level category – *small world. Small world* indicated the manner in which interaction between professional service firms and an influential client is influenced by the network of relationships that exists because of the ease of access between a specific set of organizations attentive to each other by virtue of the shared reputational capital.

In summary, this chapter presented the quantitative and qualitative data used to explore the relationship between a large client, Enron, and the professional service firms associated with it. The quantitative data analysis examined whether there existed a set of professional service firms that interacted consistently with Enron, while the qualitative analysis explored the manner in which client relations are perceived by professionals. The qualitative analytic processes led to the development of categories such as PSF ethos, ease of access, nature of decisions and small world. The following chapter will present the results based on the categories and relationships between them derived here.

Chapter 7
The Complexity of Professional-Client Relationships

Introduction

The central aim of this chapter is to explore the phenomenon of client capture using the categories and issues that emerged from the analysis in the previous chapter. I start by introducing the central concept 'the small world of professionals and clients'. The subsequent sections discuss the manner in which other categories substantiate the notion of the small world. Finally I discuss how 'small world' contributes to our understanding of client capture and professional behavior.

The Small World of Professional-Client Relationships

Client capture characterizes the relationship between large firms and large professional service firms with whom they work. it is an interesting concept for three key reasons: first, it proposes that some clients possess expertise enough to influence professional work; second, it offers the opportunity of examining the professional-client relationship from the perspective of the professional; and finally it allows for the expression of other factors that influence professional work such as the organizational forms that professionals work in. However, it is still a phenomenon that is understudied. The failure of Enron and Arthur Andersen and the subsequent criticisms of the professional service firms it associated with provide an excellent opportunity to explore client capture. Theoretically too, the Enron case requires a different approach; Enron as a large organization had several simultaneous projects involving many professional service firms therefore the traditional dyadic approach would be inadequate to explain the event .Enron was also a large corporation associating with similar large and prestigious professional service firms so the traditional asymmetry of power approach of examining professional-client relationships would not entirely explain the case. The above reasons necessitated a more inductive approach towards understanding the manner in which a large client and large professional service firms negotiate their relationship.

One of the most surprising observations that emerged from the analysis of the Congressional Hearing transcripts was the extent to which professionals relied, believed, and corroborated the client's, i.e. Enron's, version of its financial health despite possessing enough expertise and having access to information that would have contradicted the client's version. This kind of relationship where a group of professional service firms are connected to each other through a common client, and interact on a regular basis with each other and the client, was termed as the small world.

Traditionally the concept of the small world refers to a special kind of network that is highly locally clustered and has a short path length, i.e. it is a kind of network where actors/nodes are not only connected to each other but are also connected by persons who know each other well enough through past collaborations or through having collaborations with common third parties. Small worlds have significant consequences on the manner in which information is accessed, processed, and acted on (Davis, Yoo and Baker, 2003; Uzzi and Spiro, 2005). This study suggests that one of the salient consequences of the small world of professional and clients is the tendency to base professional work not on available factual information but one that depends heavily on the version presented by the client. The concept of small world of professionals and clients is interesting because the extent of interaction between these participants influences professional decision making and professional output thus challenging the traditional premise of professional accountability and public responsibility. The small world phenomenon consists of two main characteristics: *insularity* and *decisions made on the basis of informal information*. There are five antecedents to the small world: field levels interactions; ease of access; reputation; reciprocity; and PSF ethos. The relationship between these variable is shown in Figure 7A

The present section starts with a discussion of the two main characteristic, insularity and decisions made on the basis of informal information; followed by subsequent sections that discuss the role of the antecedents in creating the small world of professionals and clients. The next few extracts will illustrate and explain the manner in which these two key traits contribute to the sustenance of the small world of professionals and clients.

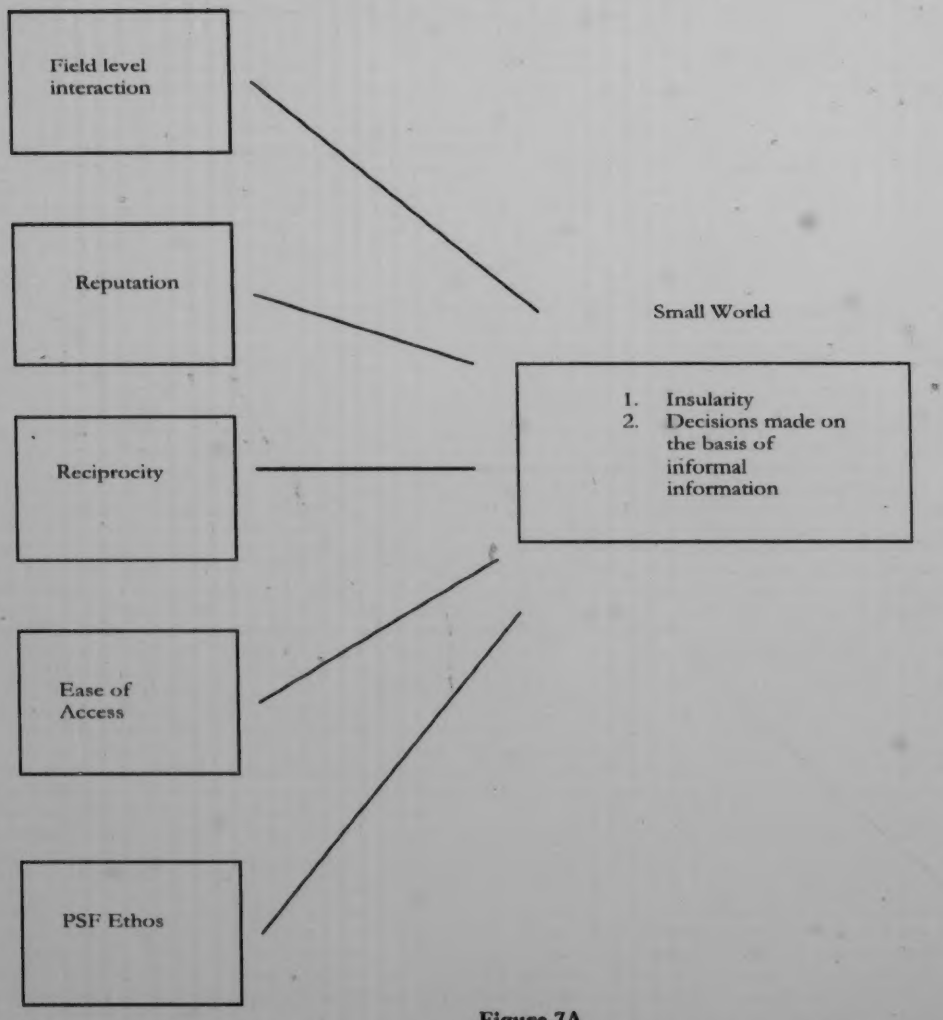

Figure 7A

The Small world of professionals and clients: Antecedents and Constitutive Traits

(i) Insularity in the small world of professionals and clients: Insularity refers to the tendency of the participants to remain immune to any information except what is exchanged between them, as the following extract suggests:

> **Senator Collins**: Mr. Prince, I do recognize the steps that you have taken since our last hearings to put additional safeguards in place and I don't minimize those actions. I think they do represent progress. But in looking at the documents involved in these transactions, I find it very difficult to understand how these transactions were approved under your old procedures…In one e-mail, for example, an Alan McDonald says, "We, Bill Fox and I, share risk's view and if anything feel more strongly that the suitability issues and related risks, when coupled with returns, make it unattractive"
> Another e-mail describes one of these transaction as "a funky deal accounting-wise," and characterizes another Citigroup employee's view as being "amazed that they can get it off the balance sheet." …How did this happen? Why would these transactions all be approved when

you have so many red flags, describing the accounting as "funky," saying that they don't understand how this achieves Enron's objectives of getting off-the books treatment for these transactions, saying that a lot of exceptions were made to standard policies? How could this have happened under your old procedures?
Mr. Prince: Senator, I will tell you honestly, I have doné a lot of soul searching about that. I think, honestly, that our people did spot some of those issues, did raise them. You have quoted the various documents. And I think that in hindsight, our people were too comfortable with what was told to us by the outside auditors, the law firms that structured and closed these transactions, and Enron themselves. I think that at that time we did not view ourselves as being responsible for what Enron did with its own books.

In the above extract, Congressional Representatives question Citigroup professionals about their decision to approve the financial structures created by Enron despite the knowledge that the information provided by Enron may not be completely reliable. The professional's explanation suggests that their final decision making was based more on the opinion of the client's outside auditors and law firms than on their professional evaluation.

Insularity operates in two key ways: it is not only the tendency to be attentive to certain sources of information but also suggests a certain lack of attention to examining the credibility or the basis of that information, as the extract below indicates:

Mr. Pellecchia: I believe what I was asked was exactly how does Enron make its money, and my response was, "Do you have a year?" That was--
Senator Bunning: In other words--
Mr. Pellecchia: That was a glib answer. But the spirit--
Senator Bunning: OK. I know it is a glib answer, but you are responsible for the ability to grade that either investment grade security or non-investment grade security.
Mr. Pellecchia: Yes.
Senator Bunning: And you are making light of the fact that you are not sure how they are making their money?
Mr. Pellecchia: Well, I think the spirit of the answer was Enron's a big company, it's a complex company--

In the above extract the professional's comments about Enron's financial activities indicates indifference to understanding how their client operates. It reinforces the notion of insularity where nothing but a preferred source of information, here the client, holds any credibility. So, when Enron says that they are a complex company with complicated financial arrangements, it's an argument that PSFs interacting with Enron unquestioningly accept.

It is important to remember that the small world phenomenon is not composed only of dyadic relationships between a PSF and a client (though the dyadic relationships reinforce it), it consists of a group of PSFs organized around the nucleus of a prized client. And it is not

only the interaction with the client that contributes to the small world approach but also the interaction between the PSFs that enforces the insularity. The extract below provides an illustration.

> **Senator DeGette**: If the allegation is that the accounting is funny, and you rely on the accounting to come to your conclusion, how can you conclude that there's not a problem with the accounting without any kind of outside analysis?
> **Mr. Dilg:** We were concerned with making sure that Arthur Andersen had at their disposal all the material facts relating to the transactions and we did try to verify that.
> **Senator DeGette:** And did you find that out? Did they?
> **Mr. Dilg**: Yes.
> **Senator DeGette**: How did you find that out?
> **Mr. Dilg:** We gave them Ms. Watkins' letter and walked through with their engagement partners point by point under Ms. Watkins' letter and--
> **Senator DeGette**: Did they have the information, so, from that you concluded yes?
> **Mr. Dilg:** They were very well aware of the issues that she was raising and that they felt very comfortable with the accounting decisions they had made in connection with the transaction.
> **Senator DeGette**: Let me ask you this, did you ask Andersen to provide you a detailed analysis of the allegations that Ms. Watkins made in her memo, most specifically, the Raptor deals and the other deals? Did you ask them for a detailed analysis or did you just say, does this look okay to you and they said yes, and that was it?
> **Mr. Dilg:** We gave them the letter, I believe, a day or so before a meeting that we had with Mr. Duncan and Ms. Cash. We did not ask for a detailed, written analysis.
> **Senator DeGette**: So you don't know to this day what Arthur Andersen's analysis would have been of the transactions that formed the basis of Ms. Watkins' concerns?
> **Mr. Dilg:** Arthur Andersen had included those transactions in the scope of their overall audit of the company and they confirmed to us verbally that they were still comfortable--
> **Senator DeGette**: This seems like an incredible circle to me. She says well, there's problems with the audit, so you go ask the people that did the audit. They say the audit was okay, so it just comes back to point one.
> How could you decide independently if it was true or not?
> **Mr. Dilg:** We could not decide on whether the accounting was correct. We're not in position to do that. We could decide whether the Big Five accounting firm that the company's audit committee had decided to rely on for accounting advice were aware of the concerns and that they were still satisfied with their accounting advice

In the extract, lawyers in Vinson & Elkins are asked by Enron to investigate the concerns bought forward by some professionals in Enron regarding accounting procedures and financial structures in which Arthur Andersen played an important role. Vinson & Elkins approach the investigation not in the spirit of conducting professional due diligence but more as an endeavor of justifying decisions made by the client. First, they decide to limit the scope of the investigation in consultation with the client; second, the lawyers instead of investigating, take those very concerns to Arthur Andersen to ask if they are comfortable with the decisions they took. On receiving an affirmative answer, the investigation is over. The extract illustrates further the insular nature of the small world. In this case, the interaction is between two PSFs dealing with the same client. Both, Arthur Andersen and

Vinson & Elkins, appear to alter the idea of professional diligence into a client centric endeavor. Arthur Andersen did it in advising Enron on the financial structures, and in promoting certain accounting choices; Vinson & Elkins in turn converted the investigation into an assurance providing mission to the client.

One of the more disturbing indicators of insularity inherent in the small world is the tendency of professionals to reframe available information to suit the client's perspective, i.e. even though they may have information that points in a certain direction, they are likely to view or interpret it in a manner that is more client centric.

> **Senator Greenwood:** Well, let us talk about bad cosmetics. During the course of your inquiry, you interviewed Jeffrey McMahon. In the summary of Mr. McMahon's first interview on August 30, 2001, with you, you note that he indicated that some bankers thought there might be linkage between investing in LJM and future business with Enron.
> In his second interview with you conducted on October 18, 2001, a few days after you submitted your report, Mr. McMahon told you of specific instances where investment bankers complained to him of being pressured to invest in LJM transactions, or were promised Enron business if they invested in LJM.
> Mr. McMahon identified specific institutions-First Union, Merrill Lynch, Deutsche Bank, Chase Bank-and specific bankers, including Paul Riddle, and provided the names of Enron employees who could provide additional information on this subject-Ben Glisan, Tim Despain, Ray Bowen, and Kelly Booth. This subcommittee has learned of other individual bankers who have complained. In your October 15, 2001, letter to Mr. Derrick, you wrote, "The second potential conflict of interest identified by several individuals was that investors in LJM may have perceived that their investment was required to establish or maintain other business relations with Enron. Although no investors in LJM were interviewed, both Mr. Fastow and Mr. McMahon stated unequivocally that they had told potential investors that there was no tie-in between LJM investment and Enron business."
> Your description of what you had learned appears to be highly misleading. Mr. McMahon clearly indicated in his first report that some banks-that there was a linkage, and that someone at Enron had made these promises. Presumably, given his position, it was Mr. Fastow. But you make it appear as if they are both shooting down this allegation when, in fact, it was Mr. McMahon who raised the allegation. And he clearly had names of individuals and banks as set forth in the summary of the second interview.
> Based on the facts you knew at the time you submitted the report, why isn't your description misleading?
> **Mr. Dilg:** I don't believe our description is misleading, Mr. Greenwood. We did want to alert the company to the concerns raised, I think both by Ms. Watkins and Mr. McMahon, that they had heard that there was linkage. Mr. McMahon told us that he had told any banker that asked him that there was no linkage. Mr. Fastow also adamantly denied any linkage.
> The concerns we heard raised were some people within investment banking and commercial banking institutions grumbling because they didn't get deals that they thought they were supposed to get because they invested in LJM, which indicated—

The above extract is an example where information available to professionals is reframed in a client centric manner. Here, the lawyers from Vinson & Elkins who were investigating concerns raised by employees at Enron explore the allegations that the Enron CFO Andrew

Fastow pressured investment banks to invest in the particular financial structure he had come up with. In spite of getting information that corroborated this information, the lawyers chose to focus on aspects of the information that enabled them to interpret it as disgruntled investment bankers expressing their grouse for not having the opportunity to invest in the financial structure. This kind of reinterpretation of information to support a particular version further strengthens the insularity trait in the small world phenomenon.

Another indicator of insularity is the manner in which the participants actively attempt to transform concern raising information as 'normal'.

> **Senator Levin:** You had earlier, in Exhibit 322(g),1 in a memo, you were aware of the fact that this highly reliable company, one of the largest in the country, significantly dresses up its balance sheets at year end. You were very much aware of Enron being someone who liked to and was willing to and typically did dress up their balance sheets, because you wrote in that memo that is at Exhibit 322(g) that, "based on 1999 numbers, it would appear that Enron significantly dresses up its balance sheet for the year end. Suspect we can expect the same this year."
> So you were expecting a dressing up, disguise, costume by Enron at the end of the year 2000. You had received strong suggestions from other Citi relationship managers that it was possible that Citi would claim earnings from the Bacchus transaction. You were told only apparently-you are supposed to be in a position here of some decision making import-you were told that it was-you just took Enron's word that it was unlikely that there would be an earnings impact. How can you explain that?
> **Mr. Fox:** Let me comment and address that, Senator. My reference to dressing up the balance sheet is a slang reference that a number of companies will take certain steps at various points in their financial cycle to address balance sheet targets. They can stretch out payables to generate cash. They can monetize or securitize receivables to generate cash and pay down debt. They can borrow under their bank facilities and pay down short-term commercial paper. Many steps that large financial-I mean, large Fortune 500 companies take to impact their balance sheet.
> The context here was that I was looking at their September 1999 financial statements, reviewed them, and if I recall correctly, the debt-to-capital ratio appeared higher than it would at year end and that seemed to indicate to me that they would take certain steps as it impacts their balance sheet. That was a balance sheet comment and statement. It was not related to the income.
> Remember, at the time, Enron was an important relationship. Enron was a highly respected company. We had no reason to suspect or believe that we could not trust and accept their word.

In the extract, Congressional Representatives try to understand why despite knowing that Enron has a history of bolstering its financial statements through questionable decisions, did Citigroup go ahead with their association. Citigroup tries to make an argument that as most large prestigious firms (Fortune 500) indulge in such practices, these are seen as 'normal' practices by the PSFs. There are three important things to note here: first, Citigroup tries to suggest that as most large and prestigious firms practice the 'dressing up' therefore such

practices are not troubling; second, as Citigroup shared a special relationship with Enron, it appeared logical for them to trust Enron's word, i.e. professionals who have had a long term relationship with certain clients are more likely to neglect the process of professional due diligence and accept the client's version of the information. Finally, the above extract also highlights the fact that the insular trait within the small world phenomenon is not an unconscious phenomenon that happens over time but more a cumulative effect of active choices that professionals make regarding the relationship.

(ii) Decisions made on the basis of informal information and small worlds: The second key trait evident in the small world phenomenon is the strong tendency of professionals to make decisions based on informal information. Here participants in the small world privilege not only certain sources of information (i.e. information that comes from participants), but also particular channels (i.e. information gleaned through personal contact and communication). Some examples of professional decision making based on informal information are presented below.

> **Senator Levin:** Mr. Fox, you told the Subcommittee staff that Citi had a business policy that it would not engage in structural transactions that had a material impact on reported net income. That was the business policy that you had, and that Citi would look further at the project and assure itself that the project would not impact reported net income. That was your policy in place at the time.
> Yet, throughout the Bacchus transaction, you were notified that there was a possibility that Enron would use the transaction to report net income in its year 2000 financial statement…on December 6, there is an e-mail, Exhibit 322(d), [3] which states, "It is probable that the monetization will add to funds flow from operations as a portion of the assets will be from merchant pool. It is possible but not certain that there will be earnings impact." That was the last communication on the matter.
> Now, did the Citibank policy then require further investigation at that time, since there was the possibility of an earnings impact which your policy would not permit?
> **Mr. Fox:** Senator, the series of e-mails you referred to, starting with the first one, certainly highlighted the potential of an earnings impact. We went back to the company. We went back to the treasurer of the company, who confirmed to us that there would not be significant material earnings impact.
> **Senator Levin:** So that you specifically contacted Enron after your decision that there could be an earnings impact to see whether there would be and they told you there would not be?
> **Mr. Fox:** I did not specifically contact them.
> **Senator Levin:** Who did?
> **Mr. Fox:** Jim Reilly, who is a Managing Director of our firm. If you go further into that last e-mail you made reference to, he reports that Enron has suggested, however, that because of their ongoing involvement in the business, it is unlikely there will be any material earnings benefit.
> **Senator Levin:** And you accepted that without further investigation?
> **Mr. Fox:** We relied on Enron's word. They were a company we had a good relationship with at the time and that is something we would have relied on, yes, Senator.

In the above extract, professional decision making appears to be guided more by the *nature* and the *source of* information coming from the client. Congressional Representatives ask senior professionals from Citigroup about participating in some of the financial structures that Enron proposed. Despite knowing two key pieces of information – first, that the proposed financial structure may have an impact on Enron's earnings by making it look better than it actually was; and, second, that participating in financial structures that impact client's earnings statement was against the policy of the investment bank - senior professionals went ahead and approved the transaction. When asked, their reason was that they approached the client firm to clarify whether it would influence the earnings, and on receiving their reassurance they moved ahead with the transaction. This textual extract is very interesting because it illustrates that although professionals possess the expertise and informational cues that would allow them to take different decisions, they *choose* to go to the client for clarification and then proceed with the transaction thus indicating that they were more inclined to believe the client's version rather than rely on their own due diligence.

The strength of the small world phenomenon is also discerned by the fact that professionals at times based their entire decision making and output on the verbal assurance provided by the client.

> **Senator Collins:** I have to tell you that I read it exactly the opposite. If it was important enough for you to go and meet with Andrew Fastow to get that commitment, and if it appears four times in the approval memorandum, and when there is actually a statement in this memorandum saying that the equity risk is largely mitigated by the verbal support received from Enron, how can you continue to maintain that this commitment really had no meaning?
> **Mr. Fox:** I think that is just the point, Senator. It was mitigated, not eliminated. We had that risk, and I think that is what we were highlighting to everyone, so that everyone in our firm who was approving the transaction understood that this was an incremental risk we were undertaking.
> **Senator Collins:** On Exhibit 366,[1] the phrase is used that it is a verbal guarantee and the percentage is 100 percent. What does that mean.
> **Mr. Fox:** Senator, I am sorry. Where are you exactly in the exhibit?
> **Senator Collins:** It is Exhibit 366. It is under "Support" typed to the left. It says, "verbal guarantees," "Enron Corporation," "percentage: 100."
> **Mr. Fox:** Yes, I am sorry.

The above extract illustrates an instance where it appears as if professional output is more a result of the degree of closeness between clients and professionals rather than a process of evaluation of information by experts. Congressional Representatives attempt to understand the basis for structuring an agreement between the investment bank and Enron. The

investment bank is supposed to have invested money in a structure created by Enron where lawfully the money would have been at risk. The bank in order to reduce the risk of losing the money gets the verbal support of Enron's chief financial officer, Andrew Fastow, who assures them that their money will not turn into a loss. Citibank decides to go ahead with the structure, drafting the agreement based on the CFO's verbal support. The extract indicates two key aspects of the small world phenomenon: first, professional decision making does not appear to be any different from the decision making that would occur in a well bound clique where participants would cater *only* to each other's mutual benefit. Second, because professional decision making gets divorced from due diligence that characterizes it, the questionable appropriateness of designing and executing financial structures based on informal information, is never raised.

Small worlds comprised of a set of PSFs and clients not only influence professional decision making in their own organizations but also have consequences for individual and institutional investors, as the following extract shows.

> **Mr. Diaz:** Certainly we were aware of the triggers. I'd just like to point out one thing. When we held our rating committee-I think it was November 7; it's in the record if I'm incorrect-that evening, we concluded that we would downgrade Enron to Ba2, non-investment grade, and we were ready to put that press release out the next day. We were aware of the consequences to Enron, yet we made that decision.
> The reason that we ultimately did not bring it down to non-investment grade had to do with the changes they made in the merger agreement and the additional equity they were willing to put in. And that's why we ended up with a Baa3 rating as opposed to Ba2. But we were aware of the circumstances, and that would not have stopped us from downgrading to below investment grade because we felt that fundamentally the company no longer merited that rating.
> **Senator Bennett:** So the thing that saved your rating and gave them a temporary reprieve from the harshest of all triggers was your conviction that the merger was going to give them sufficient capital to survive?
> **Mr. Diaz:** Three things: That the merger would give them the capital to survive; the probability that the merger would go through based on the changes they had made; and that the combined entity would be investment grade because of the structural changes they made to the deal.
> **Senator Bennett:** Well, those are all three if's. In order for the thing to make it, all three have to fall in place. If any one of them falls out of place, the whole thing collapses.
> Now, we are here with the brilliance of hindsight, and I recognize that and don't want to put myself in your position when you are trying to look at it in foresight. But it does seem to me, to just summarize it, in order for Enron to avoid the disaster of the non-investment grade rating, three things have to happen. There is no absolute assurance-of course, I guess in this world there is no absolute assurance of anything. It was your judgment that it was likely that all three would happen.

In the above extract the professionals in a credit rating agency explain why it continued to recommend Enron as an investment grade firm despite the low stock prices and general concern about Enron's financial health. The rating agency justifies its decisions based on two

key pieces of information: first, their discussion with Enron's top management who assured them that all concerns were taken care of; and second, the confidential information that indicated that Enron had the potential to recover after the possible merger with Dynergy. However, there is a crucial issue to take note of: that is, there are several conditions to be fulfilled before the merger between Enron and Dynergy could be completed, making the merger a very tentative possibility. This raises questions about the basis on which the credit rating agency continued to continue to recommend Enron as an investment grade stock. More troubling is the realization that the final decision to continue endorsing Enron's status was not based on professional evaluation of the firm's financial health but *solely* on the assurance given by the top management at Enron.

Summary. The above discussion focused on elaborating the small world of professionals and their client. Traditionally small worlds are seen as networks of organizations or people who are connected through multiple channels. For example, if one considers the social space of large client firms such as Enron and large PSFs, it is possible to envisage that larger firms are more likely to share connections with larger PSFs. Also large PSFs are more likely to come in contact with each other while working with large client firms. Small worlds tend to have high representation of cliques where participants have a tendency to favor a preferred view of the world that is partial to the interests of the participants. The small world of professionals and clients appears to be characterized by two key traits: *insularity* and *decisions based on informal information.* Insularity, I have defined as the propensity of small worlds to base professional decision making on information available from certain preferred sources (i.e. participants of the small world). Insularity within the small world operates in several ways. It is generated by the inclination of professionals to privilege a preferred source of information. One of the biggest surprises to emerge from the analysis was that, despite access to ample publicly available cues that showed that Enron may not be in stable financial state, most PSFs associated with it *chose* to base their decisions on the information provided by the client and the other PSFs associated with Enron. A more nuanced view of insularity suggests that it is a kind of instrumental screening used by professionals to focus only on the information that is of interest to them. As indicated by the textual extracts, PSFs interacting with Enron chose to ignore available information in order to proceed with their specific projects with the client. Insularity in the small world is also reinforced when professionals

reframe or reinterpret information either in a manner that is client centric, as Vinson & Elkins did, or make even potentially disturbing information appear 'normal', as the investment banks did, in order to explain Enron's dressing up of their balance sheets.

The trait of *informality* is different from insularity in a critical way. Whereas insularity suggests that participants of the small world are impervious to the information outside the small world, *decision making based on informal information* suggests that professionals within the small world consciously privilege certain sources *and* specific channels of information. For example, in Enron's case, several of the investment banks decided to participate in the financial structures created by the client simply on the basis of the verbal support (i.e. informal) assurances provided by the Chief Financial officer. Similarly, credit rating agencies based their recommendations more on the talks they had with Enron's top management than on any sort of professional and objective evaluation of Enron's financial state.

The small world of the client and the PSFs, then, becomes really interesting because of the implications it has for professional decision making, output, and accountability. Insularity and informality of decision making suggest that professional choice consists more of negotiation and collaboration with the client about mutual interest. This picture of professionals at work contradicts the traditional view of professional work which is characterized by professional objectivity and due diligence.

The next section presents the antecedents that structure the small world. it is followed by subsequent sections that will discuss in detail the factors that reinforce the small world. I examine, in turn, the roles of: interaction; reputation, reciprocity, ease of access, and PSF ethos.

Antecedents of the small world

(i) Field Level Interactions. In order to understand how the small world of professionals and clients operates, it is important to explore its structural origins. It is by focusing on activities that bring professionals and clients together that the frequency and the patterns of interactions become evident. In the case of Enron, there were at least seven professional

service firms that participated in the Congressional Hearings. These seven firms more than others had been interacting with Enron over a period of time.

One approach to understanding how closely Enron and the seven PSFs interacted with each other is to examine the new equity deals that Enron structured from 1995-2001. New equity structures are an important and pertinent activity to focus on because they involve investment banks, accounting firms, law firms, and security analyst firms. Another reason that makes equity deals relevant is that much of the criticism of the PSFs and Enron revolved around the manner in which equity structures were designed and executed. In order to understand the frequency of interaction of the PSFs with Enron, I started by focusing on five investment banks that participated in Enron's equity structures and were present at the Congressional Hearings. These five banks were: Smith Barney (now Citigroup); Credit Suisse First Boston; Goldman Sachs &Co; JP Morgan; and Merrill Lynch. I calculated the percentage of new deals each year in which the above mentioned investment banks were underwriters and book runners. Tables 2(a) and (b) below provide the breakdown in terms of percentage of the involvement of the investment banks.

Table 7-1: Investment Banks Involved with Enron's Capital-Raising Deals.

Year	Smith Barney (now Citigroup)	Credit Suisse First Boston	Goldman Sachs & Co	JP Morgan	Merrill Lynch	Total Number of new Issues
1995	7	0	5	0	3	12
1996	2	0	2	3	1	8
1997	5	2	2	3	5	18
1998	1	4	2	1	5	14
1999	5	5	2	4	5	23
2000	4	4	0	1	3	16
2001	4	2	0	1	3	19

Table 7-2: Percentage breakdown of Investment Banks involved with Enron's Capital-Raising Deals

Year	Smith Barney (now Citigroup)	Credit Suisse First Boston	Goldman Sachs & Co	JP Morgan	Merrill Lynch
1995	58%	0%	42%	0%	25%
1996	25%	0%	25%	38%	13%
1997	28%	11%	11%	17%	28%
1998	7%	29%	14%	7%	36%
1999	22%	22%	9%	17%	22%
2000	25%	25%	0%	6%	19%
2001	21%	11%	0%	5%	16%

Table 7.1 shows the number of deals involving each investment bank. Table 7.2 presents the same information in terms of the percentages of total deals in each year from 1995-2001. As is evident from the Tables, every year there were at least two investment banks that were involved in more than twenty five percent of Enron's new equity deals. Smith Barney and Merrill Lynch, both, consistently had very high levels of participation (ranging from a minimum of seven percent to a maximum of fifty eight percent for Smith Barney; and, a minimum of six percent to a maximum of thirty six percent for Merrill Lynch). Credit Suisse First Boston garnered a large percentage of the deals from 1995-1998, and Chase from 1996-1999. What these numbers indicate is that Enron preferred some investment banks more than others and therefore interacted with them on a more frequent basis.

My next step was to examine how many of these investment firms were bookrunners in the same period in the same deals. One of the problems researchers have with an investment bank being the underwriter *and* the bookrunner for the same deal is the conflict of interest issue (Loghran and Ritter, 2004; Crowen, Groysberg, Healy, 2006). As an underwriter, the interest of the investment bank is to make sure that the new deal is structured in a way that makes it attractive for the public investor. The bookrunner on the other hand has the responsibility of ensuring that the deal is priced in the market in an objective manner, in consideration with the state of the market, competitor pricing, and other variables. Though investment banks insist that they separate the function of underwriters and bookrunners, it is an issue that is still debated. Table 7.3 provides a breakdown in terms of percentage of the investment banks which were underwriters and bookrunners for the same deals from 1995-2001.

Table 7-3: Breakdown in terms of Percentage of Investment Banks participating as both: Underwriters and Bookrunners.

Year	Smith Barney (now Citigroup)	Credit Suisse First Boston	Goldman Sachs	JP Morgan	Merrill Lynch
1995	8%	0%	42%	0%	8%
1996	0%	0%	13%	25%	13%
1997	17%	6%	6%	11%	22%
1998	14%	14%	0%	0%	21%
1999	4%	13%	13%	0%	17%
2000	19%	6%	0%	6%	31%
2001	21%	5%	0%	0%	16%

Table 7.3 shows the percentage of deals where investment banks were both underwriters and bookrunners. The patterns in Table 7.3 appear to echo that of Table 7.2. Smith Barney (Citigroup) and Merrill Lynch were involved in both roles in several of their equity deals. The other investment banks exhibit similar patterns of playing dual roles. An important insight from examining this pattern of interaction is that not only do client firms prefer certain PSFs, they also tend to interact with them at multiple levels (i.e. when PSFs take on dual roles). This observation gains more support when analysts are taken into account.

In addition to being underwriters and bookrunners for large clients such as Enron, large investment banks also have their own analyst divisions which issue recommendations for the new deals that come out in the market. When an investment bank is involved as an underwriter, and an analyst from the same firm issues recommendations, it creates a conflict of interest situation. The data for Enron and the large investment banks suggest that in several cases from 1995-2001, analysts of the banks involved as underwriters and bookrunners issued recommendation for the new capital-raising deals from Enron. Figure 7B provides illustrations of such instances.

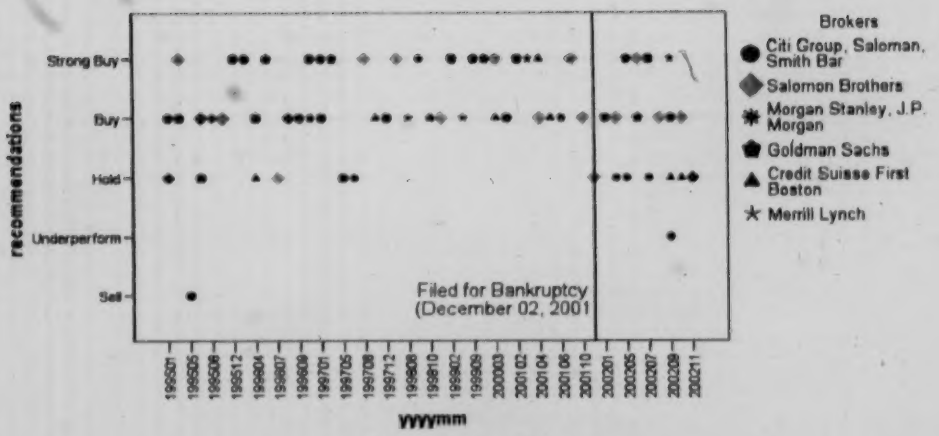

Figure 7B

Analysts' Recommendations from Investment Banks Participating as Underwriters for Enron

In Figure 7B, the X axis marks all the new equity deals from 1995- 2001 where analysts from the investment banks that were participating as underwriters *and* bookrunners were issuing recommendations for Enron. The Y axis refers to the standardized scale of recommendation used by the *SDC Platinum Database.* The higher relative density of the symbols in the 'strong buy' and 'buy' rows suggest that analysts were issuing positive recommendations for the deals their banks were involved in. One could argue that in the period from 1995-1999, Enron was outperforming most firms in its sector; therefore, the recommendations reflect its superior performance. However, it is the post bankruptcy recommendations that indicate support for research that relates positive analyst recommendations to the conflict of interest between investment banks and analysts (Rajan and Servaes, 1997; Hayward and Boekar, 1998; Demski, 2003). Despite the fact that Enron filed for bankruptcy on December 2nd 2001, it is interesting to note that there is only a slight reduction in the 'strong buy' recommendations, the density of the 'buy' row remains unaffected. In fact, up until November 2001, the only sell recommendation is given by the analysts from J.P. Morgan. In sum, Figure 7B reinforces the idea that when a client firm prefers a set of PSFs they end up interacting with each other through multiple avenues.

The same deals from 1995 to 2001 were examined for auditors and legal counsel. Table 7.4 provides the percentage breakdown of the capital-raising deals for Enron where Arthur Andersen was auditing the quality of the financial statements. As noted earlier, with many of the capital raising deals, the client firm only voluntarily submits information about auditors

and legal advisors. Therefore in the instances where the percentage is zero, the firm did not provide information about who the auditor was for the new issues.

Table 7-4: Auditors for the Capital-Raising Deals of Enron (1995-200)

Year	Arthur Andersen	Deloitte & Touche	KPMG	Total number of deals
1995	58%	0%	0%	N=12
1996	25%	0%	0%	N=8
1997	61%	0%	0%	N=18
1998	71%	0%	0%	N=14
1999	57%	4%	9%	N=23
2000	50%	0%	0%	N=16

Table 7.4 includes all the accounting firms who were mentioned as auditors for Enron's new equity deals. As Enron was not bound to volunteer information about their auditors, the list in Table 7.4 is not exhaustive. But the data available indicates the preference that Enron had for Arthur Andersen. In fact, apart from 1996, where Arthur Andersen audited two of the eight deals, in all of the other years it was involved in more than fifty percent of Enron's new equity structures.

Similarly, the client firm, i.e. Enron was not bound to submit information about their legal advisors involved in the new deals. Also, with respect to the legal counsel, the client organization can use its own in-house law department as advisors. Table 5 provides a percentage breakdown of the two law firms involved in the new capital raising deals for Enron. The first column of Table 7.5, General Counsel refers to the use of Enron's in-house law department.

Table 7-5: Legal Advisors for the Capital-Raising Deals of Enron (1995-2001)

Year	General Counsel	Richards Layton & Finger	Vinson & Elkins LLP	Total number of deals
1995	50%	0%	8%	N=12
1996	25%	0%	0%	N=8
1997	33%	0%	17%	N=18
1998	36%	0%	0%	N=14
1999	4%	0%	35%	N=23
2000	13%	6%	25%	N=16

Table 7.5 is similar to Table 7.4 in that though the data is not complete, there is enough to indicate Enron's preference for a particular law firm, apart from its own in-house law department. Except for 1996, in all the other years, Vinson & Elkins and Enron's in-house department were involved in more than fifty percent of the deals.

In sum, Tables 7.2 through 7.5 indicate that the structural origins of the small world are in frequent and close patterns of interaction. It is interesting to note that it is not merely the frequency of interaction that forms the structural basis for the small world; the quality of *closeness* comes from the interaction on multiple levels. For example, in the case of the investment banks, Enron's relationship extended not only to the investment side but also the analyst side of the bank. Similarly, Enron's relationship with Arthur Andersen was not limited to an auditor- auditee relationship but the Big Five accounting firm also consulted for Enron. These ties indicate that the small world connections operate in many interconnected ways.

A different way of discerning indirect ties between the client organization and professional service firms is by focusing on the board director affiliation. I extracted a list of the board of directors at Enron in 2000 and traced their other affiliations. *Board Analyst*, a database that aggregates director information provides all organizational affiliations. Once the information about the affiliate organizations was clear, I used the annual reports of the year 2000 which contained auditor information. Using the database and annual reports, I compiled Enron's board of director affiliations. Table 7.6 provides the directors' names, the boards they were on apart from Enron, and the auditor for the other organizations.

Table 7-6: Enron's Board of Directors, other boards they were on and auditors of the other firms

Director Name		Director Since	Board Memberships	Auditors
Robert	Belfer	1983	Belco Petroleum Corporation	Arthur Andersen
Norman	Blake, Jr.	1993	Owens Corning Corp	Arthur Andersen
			Comdisco	KPMG
Ronnie	Chan	1996	Motorola Inc	Arthur Andersen
John H.	Duncan	1985	Group 1 Automotive	Arthur Andersen
			EOG Resources	Arthur Andersen
Wendy	Gramm	1993	IBP	PricewaterhouseCoopers
Robert	Jaedicke	1985	Genecorp	Ernst & Young

Kenneth	Lay	1985	I2 tech Eli Lilly Compaq	Arthur Andersen Ernst & Young Ernst & Young
Charles	LeMaistre	1985	President, MD Andersen Cancer Center, University of Texas	Not Available
John	Mendelsohn	1999	President, MD Andersen Cancer Center, University of Texas	Not Available
Paulo V. Ferraz	Pereira	1999	Director of Group Bonzano	Arthur Andersen
Frank	Savage	1999	Lockheed Martin Qualcomm	Ernst & Young PricewaterhouseCoopers
John	Wakeham	1994	Retired Former U.K. Secretary of State for Energy and Leader of the Houses of Commons and Lords.	Not Available

Table 7.6 shows the other boards that Enron's directors were on, and the auditors for those other firms. Of the twelve directors, five were on board of other organizations that had Arthur Andersen as their external auditor. Also, of the seventeen board memberships shared between the directors, Arthur Andersen was on forty two percent of the boards. This suggests that apart from the frequency of contact that directors would have with Arthur Andersen in Enron, there were other channels where these ties were further cemented.

The above section highlighted two probable causes for the formation of the small world approach. First, a client organization that works with a specific set of professional service firms over an extensive period of time. Second, professional service firms that are involved in multiple aspects of the client's operations; for example, several of the investment banks involved in the financial structures with Enron also were issuing recommendations for the same client. Similarly, Arthur Andersen, Enron's external auditor also functioned as the accounting advisor for most of the financial structures that were created in conjunction with the investment banks. And Vinson & Elkins, the external counsel for Enron was involved as legal advisor for several of the financial structures created by Enron.

The analysis of equity raising deals, the patterns of participation of investment banks, accounting firms, law firms, and director information lead to two observations: (1) Enron as a large client interacted with a set of preferred PSFs. The interactions were frequent and persisted over the focal five year period; (2) the relationships between a large client firm and

large PSFs are not dyadic. Large firms work with several PSFs over different projects therefore professional decision making may involve more intangible variables such as ease of communication between the client and the PSFs, the attention to reputations of the participants involved and the motivation to cement the relationship be being considerate about each other's interests, than just power asymmetry between participants.

The subsequent sections focus more on the relational aspect of the small world. Specifically they examine ease of access, reputation, reciprocity, and PSF ethos to understand better the manner in which structural patterns of interactions transform into the small world phenomenon. Table 7.7 shows the number of extracts related to the relational aspects of the small world.

Table 7-7 : Number of extracts associated with relational aspects of the small world.

	Ease of Access	Reputation	Reciprocity	PSF Ethos
Number of extracts	48	57	35	84

The number of extracts in Table 7.7 indicates the relative presence of each of the relational issues. The largest number of extracts was found in the *PSF Ethos.* Most of the professionals in the Congressional Hearing were senior professionals at large PSFs, leading to frequent allusions to aspects of organizational structure, organizational goals and objectives, and perceptions of professional responsibility. These combined to create a unique picture of the distinctive spirit or culture of the organization which was termed PSF ethos. However, for me there were two relational aspects, reputation and reciprocity, that stood out during the analysis because of the *perceived* passion with which they were used.

(ii)Reputation. An intangible variable that influences and consolidates the small world phenomenon is the cumulative reputational asset between the client organization and the professional service firms. There exists broad agreement in the research on professions and networks about the competitive advantage that reputation affords. It is true especially for professional service firms where outputs are customized and intangible. Much of the confidence that a client organization has over the professional output provided by professional service firms is linked to the reputation that a PSF may command in the market.

However, where the reputation of the client organization matches or at times exceeds that of the professional service firms with which it associates, a different dynamic may occur. Enron, at its peak, was one of the largest organizations of corporate America, and was named as the most innovative company three years in a row by prestigious business media outlets (Greenwood, Li, Prakash and Deephouse 2005). Its top management personnel were celebrated as innovators and risk takers who had come up with a new and apparently sustainable business model. This reputational capital was leveraged very effectively by Enron in order to influence professional work in very distinct ways. This is indicated by the extract below.

> **Mr. Traband (Vice President, J.P. Morgan Chase)**: In addition, we would have wanted to know more about the aspects of the transactions in which the firm was not involved. But at that time, we, like many other parties, dealt with Enron in the belief that it was one of the most respected companies in America and that it was not our role to second guess our counterparties' accounting or other structuring determinations.

In the extract above the Vice President of one of the largest investment banks in the world explains the basis on which his firm agreed to participate in the financial structures that Enron created. Enron's reputation in a way served as a buffering device against professional scrutiny. Within the small world phenomenon, it is not only the reputation of the client that impedes professional scrutiny; the reputational capital associated with other professional service firms also influences the manner in which each PSF deals with professional decision making. This sensitiveness to the reputations of others associated with the client is suggested in the extract below.

> **Mr Prince (CEO, Citigroup):** First, though, let me say a few words about the specific transactions under review. While I believe our people acted in good faith, I think it is fair to say that we never anticipated that a financial intermediary like Citigroup would be criticized for the accuracy of the accounting treatment that a Fortune 10 company gave to its transactions with the express approval of a then-highly respected Big Five accounting firm. At the time we entered into these transactions, we never imagined that Arthur Andersen wouldn't even exist a year later or that a failure of ethics would have destroyed Enron, a company ranked in the top 20 on the list of most admired companies in the year 2001.

In the above extract, the CEO of Citigroup, one of the largest investment banks in the world tries to answer Congressional Representatives' queries about professional lapse in judgment. Mr. Prince reasons that it was 'good faith' that guided Citigroup professionals to partner with Enron. And this 'good faith' was based primarily on the reputations of the organizations with which Citigroup associated.

In highlighting that Citigroup was dealing with a Fortune 10 company that was working with a Big Five accounting firm, Mr. Prince attempts to build on the argument that these rankings and media cues are indicators of firm expertise and trustworthiness. In fact, through much of the Congressional Hearings, several of the professional service firms frequently defended their lack of due diligence by highlighting the reputation of the client and the other firms with which it associated, as the extract below indicates.

> **Senator Levin:** If you look at Exhibit 333(d),[1] which is an e-mail to you, Perwein, who is a Citi tax attorney, is quoted as saying that "Sundance was a funky deal accounting-wise, and was amazed that Enron can get it off the balance sheet." Do you remember getting this?
> **Mr. Caplan:** I do.
> **Senator Levin**: Do you have any reason to disagree with that?
> **Mr. Caplan:** With-I am sorry.
> **Senator Levin**. With the statement that it is amazing that they could get this off the balance sheet.
> **Mr. Caplan:** I am not an accountant. Neither is Mr. Perwein—
> **Senator Levin**. You were aware of this tax attorney's conclusion that it was a funky deal accounting-wise and amazing that Enron could get it off their balance sheet, is that right? You were aware of that?
> **Mr. Caplan:** Again, I think that is an accounting determination made by Arthur Andersen on how the structure should work. They were fully aware of all of the terms of the preferred investment. In December 2000, when the Fishtail transaction was agreed to, the firm had no reason to believe that any such determinations were not being made by Enron and/or Arthur Andersen, which was then one of the Nation's premier accounting firms, in accordance with Generally Accepted Accounting Principles.

In the above extract the Congressional Representatives ask senior professionals from J.P. Morgan why, despite indications that Enron's financial structures appeared questionable, did the bank go ahead with the partnership. Senior officials argue for their own lack of culpability by emphasizing the reputation not only of Enron but also of Arthur Andersen. The bank argues that the terms and conditions of the financial structure were well understood by all the parties involved and, given Arthur Andersen's involvement, the bank assumed that the due diligence would be taken care of.

The use of reputation as a buffer against due diligence can be seen in two ways. The above extract was an example where the terms and conditions of the preferred equity structure are so well understood that it is taken for granted that one of the participants would do the due diligence. Reputation also functions as a buffer against due diligence in the exact opposite case, i.e. in instances where the structures are new or innovative, as the following extract illustrates:

> **Mr. Caplan:** In addition, the way that this transaction was structured was presented to us by Enron and it was a combination of things. It was a combination of this preferred equity investment, which had the full blessing of Arthur Andersen, and my understanding was the more important test was not just that we had an equity investment, but that we had voting rights in the structure, and we had 50

> percent of the voting rights. We had the ability to control the destiny of the entity, and if we were a creditor of the entity, that would not be true. So I will absolutely submit to you that this is a preferred investment. It operates much like many other preferred investments out there, and it was not our accounting judgment as to how-as to whether this worked or not. This is an area of-I would call this joint venture accounting, is an area of accounting that there isn't a lot of literature on point and the way that our understanding is, that joint ventures are accounted for, is that the Big Five accounting-or Big Four now-accounting firms that give guidance, and this was Arthur Andersen's guidance on how to account for this transaction.

In the above extract, a senior official from Citibank attempts to explain why Citigroup accepted Enron's financial structures without examining it thoroughly. The main reason given for such a decision is that the financial structure is an innovative use of the more traditional preferred equity structures. Given the absence of literature and established precedence, the bank suggests that it was justified in relying on the opinion of one of the largest accounting firms in the world.

Reputation, then, contributes to the small world in two major ways. Much in agreement with extant literature, the constant reference to either the client's reputation or to the reputation of the other professional service firms suggests an acknowledgement of expertise and therefore trust in the judgment of these participants. However, in the case of professional-client relationships such trust and acknowledgement leads to the neglect of a very basic expectation of professional decision making – due diligence. Within the context of the small world phenomenon, allusions to reputational capital of participants function as buffering mechanisms impeding professional scrutiny. When the professional output is well understood and well established, reputation causes participants to be lax because everybody expects that the other is familiar with the rules. In the case of an innovative output, reputation provides a reasonable basis for refraining from professional scrutiny.

(iii) Reciprocity. Up until now the greater part of the discussion of the relationship between Enron and the professional service firms has revolved around the manner in which structural conditions, and perceptions of reputation influenced professional decision making. However, this discussion would remain incomplete if the role of the interests of the participants is not acknowledged. Extant literature on professional-client relationships highlights the asymmetry of power between the client and the professional to explain professional outcomes that favors either the client or the professional. In the case of Enron and the professional service firms, the asymmetry of power becomes difficult to trace

because of the comparable size, reputation, and expertise available within all of the participants. Therefore, the power to leverage interest becomes an important factor in understanding the manner in which the small world phenomenon gets reinforced. And it is also important to understand that the interests leveraged are not solely of the client organization. The extract below provides an illustration.

> **Senator Levin:** Citibank also had a guaranteed return interest rate, and I would like you to look at one Citi e-mail, Exhibit 333(i),[1] which appears to me to be an accurate summation of Citibank's so-called investment in Sundance. It is supposed to be an investment at risk. Principal is supposed to be at risk. Here is what the e-mail from Citibank says. "Still an equity investment of sorts, accounting and tax basis for partnership, but it is structured in such a way that the 670 basis points are guaranteed or we blow the deal. Also, our invest," I assume that means investment, "is so subordinated and controlled," and now these are the key words, "that it is unimaginable how our principal is not returned," Unimaginable how the principal could not be returned.
> This is supposed to be an investment at risk. Guaranteed return interest. Unimaginable, in your own words, how your principal would not be returned. Now, how does one realistically say that funds are at risk under those circumstances so that Enron could keep Sundance off its balance sheet?
> **Mr. Caplan:** Well, I would say a few things. First, I think it is important to note that this structure was presented to us by Enron in exactly this form, and our investment was absolutely in a preferred position. It was senior to Enron's investment. They absolutely had to lose $700 million. But my choice of words would not be "unimaginable." There were many circumstances that we ran through--
> **Senator Levin:** OK. So your employee described this as unimaginable.
> **Mr. Caplan:** But we spent a fair amount of time going through scenarios in which we could lose our money in this transaction. Now, I will submit to you that they are remote scenarios, but nevertheless, they are real. For example, one of the assets in this partnership was a paper mill in Canada sitting on the St. Lawrence River. If that paper mill blew up and caused significant environmental damage, we would have-our return would have been subordinated to the liability caused by that damage, and that was something we were very concerned with in this transaction.
> **Senator Levin:** Was there insurance on the paper mill, by the way?
> **Mr. Caplan:** I believe that there was insurance on the paper mill.
> **Senator Levin:** So the risk here was that the paper mill would blow up. That risk was covered by insurance. Get to some real risk here, will you?

The extract above is a telling example of the manner in which large professional service firms can use their expertise to achieve advantageous deals for themselves. In this instance the client, Enron, needed an equity loan where the principal amount would be at risk so that returns from the loan structure could be shown as earnings in the financial statement. Citibank agreed to the loan arrangement but structured it in a way that the principal amount was never really at risk. The equity structure in its present setting would have ensured that the probability of Citigroup's investment being at real risk was extremely low. It is important to note that in this instance both Enron and Citigroup were catering to their interests - Enron needed the equity loan to make its financial statement appear healthy, Citigroup was ready to lend the money but wanted to ensure that their investment remained protected. Another textual extract illustrates the enmeshing of mutual interests further.

> **Senator Collins:** Mr. Prince, how much was this driven by the fact that there was the lure of big fees? I come back to this e-mail, and it is Exhibit 322(i),[1] where it says, "Sounds like we made a lot of exceptions to our standard policies. I'm sure we've gone out of our way to let them know that we're bending over backwards for them. Let's remember to collect this IOU when it really counts." What does that mean to you?
> **Mr. Prince:** Well, Senator, as you know, I was not managing this business and I wasn't intimately involved in these transactions, but in being briefed on these transactions, my understanding is that the exceptions to our policies involved things like choice of law, whether it is Texas law or New York law, things like that.
> But the short answer is, I can't put myself in the minds of the people who did these transactions.

In the above extract the leveraging of interests between professionals and client becomes much more apparent. In this case Enron needed the investment banks to participate in financial structures devised by their external auditors and counsel. Many of these financial structures were extremely new and did not have established procedures and practices that had disseminated broadly. In such instances, other PSFs, such as investment banks, choose to sideline organizational policies and standardized professional practices in order to participate. Much as they were trying to maintain their relationship with a long term and valued client, the extract also outlines other motivations that play into the relationship.

Higher fees appeared to be another motivation which played into the relationship. As the financial structures got more complicated, investment banks could charge higher processing fees. Further, the allusion to 'IOUs' suggests that professionals and clients view the relationship as a dynamic one where the expectation is that, at appropriate times, both professionals and the client will accommodate each other's interests. In fact in some instances, when the general interest of the small world appears to get threatened, the participants band together to redefine the situation.

> **Senator Thompson:** I noticed here that on November 8, after reviewing a copy of the merger terms, the merger with Dynegy, you were concerned there were too many conditions that would allow parties to walk away from the merger, and Moody's informed Enron that it might drop its rating to below investment grade. Subsequently, Moody's received a number of telephone calls from interested parties, including Richard Grasso, CEO of the New York Stock Exchange, Robert Rubin of Citibank, Michael Carpenter of Salomon Smith Barney, and William Harrison of J.P. Morgan Chase. The banks assured Moody's that they were not planning on getting out of the merger. Again, the next day, Moody's downgraded Enron, but not below investment grade. Clearly, Enron had called all these investment bankers up to get them to call you, right?
> **Mr Diaz:** Well, the bankers did but I think they only wanted to assure us that they were serious about the merger.

In the above extract, when Moody's contemplated reducing Enron's rating to below investment grade, the professional service firms involved with Enron and who knew about the merger with Dynergy got in touch with the credit rating agency to assure them of their seriousness of supporting Enron through this process. An important aspect to note is that the reinforcement of mutual interests is central to the survival of the small world. And the mutual interests are maintained through the dynamic of give and take.

> **Senator Levin:** But Chase agreed to recharacterize something as a loan to it instead of a loan from it in order to help Enron avoid taxes.
> **Mr. Peiffer:** I think in order to, under the Canadian tax rules, potentially avoid withholding taxes if the transaction were-if the tax benefits with respect to the transaction were disallowed. That doesn't take away the strength of the opinions or what we or Enron believed to be the high probability of the tax benefits.
> **Senator Levin:** There is nothing to take away from those opinions, because you knew-Chase knew that this loan was not $1.4 billion. That much, we know you knew. You have acknowledged that. You knew it was an economic loan of $400 million.
> **Mr. Peiffer:** It was an economic loan of $375 million--
> **Senator Levin:** Three-hundred-and-seventy-five million.
> **Mr. Peiffer:** [continuing]. For legal and Canadian tax purposes, the advice we received is that it was, indeed, a $1.4 billion loan.
> **Senator Levin:** And you also knew that it was going to be challenged or could be challenged, and you also then agreed with Enron that if it were challenged, you would retroactively change its nature. You would recharacterize it so that Enron wouldn't be hit with taxes by Canada. You helped to perpetrate a fiction. You helped them perpetrate a fiction, because there was no $1 billion loan.
> **Senator Levin:** That is a fiction. There was no $1 billion lent to them.
> **Mr. Peiffer:** We have opinions from Canadian tax counsel--
> **Senator Levin:** Was $1 billion lent to them or not?
> **Mr. Peiffer:** [continuing]. With that--
> **Senator Levin:** Was $1 billion lent to them? I know there was $375 million. I am not talking about that. Was there $1 billion lent?
> **Mr. Peiffer:** There was a $1.4 billion loan made to the subsidiary of--
> **Senator Levin:** Of which $1 billion was repaid within minutes, is that--
> **Mr. Peiffer:** Under a separate contract, with money coming from elsewhere in Enron.
> **Senator Levin:** Separate contract, it was repaid within minutes, wasn't it?

The above extract is a very clear example of the manner by which professional service firms keenly and aggressively negotiate their interests with the client while ensuring that the client's interests are maintained. The above extract refers to Enron's investment in Canada with the help of an investment bank, J P Morgan Chase. One of the reasons and incentives for investing in Canada was the tax benefits that would accrue to Enron. However, to gain the benefits and savings, Arthur Andersen advised that the loan amount from J P Morgan Chase should be close to U.S.$1.4 billion. In concurrence with all the participants, it was agreed that Chase would loan U.S.$375 million to Enron, termed cleverly as 'economic loan', while the rest of the loan, close to U.S.$ 1billion, was transferred from Chase to Enron, officially acknowledged as a loan, and then immediately paid back to Chase. This kind of catering of

mutual interests between the client firm and PSFs on the one hand raises questions about the appropriateness of such transactions, and on the other, highlights the importance of understanding the nuances of professional-client relationships.

The above discussion suggests that the cement that glues the small world phenomenon together is a shared understanding that professional and client interests are mutually constituted and executed. Mutual interests are negotiated through professional decision making raising questions about one of the most dominant assumptions related to professional work – that professionals maintain distance and objectivity from clients in order to create professional output that is accountable to the outside investor. In fact, throughout the Congressional Hearings a pervasive theme in the discussion of the financial and equity structures designed by Enron, the investment banks, law firms and accounting firms, was the extent of negotiation that went on between participants to ensure that all of their interests were catered to in the process. In some cases where the professional service firms had to set aside organizational policies and practices to ensure that the client's interest was taken of, they were cognizant of the favor they were doing and were vocal about ensuring that they in return would receive similar consideration from the client. Reputation and reciprocity consolidate the small world which is strengthened when professionals have easy access to their client.

(iv) Ease of Access. The professional service firms with which Enron dealt were large and had many clients therefore client preference could not have been the sole determinant of professional (mis)behavior in these firms. It is important to examine other variables that engender the traits of insularity and the tendency of professionals to make decisions based on informal information.

One of the key variables emerging from the data that contributes to the small world phenomenon is the ease of access between professionals and clients. Ease of access taps into the notion that some professional service firms, by virtue of their association with their client, are given/gain direct access to the client. In such cases when the professional service firm needs clarification, its first recourse is the client and not publicly available information about the client. The following textual extract illustrates an instance.

Mr. Barone: Thank you, Senator. The confidence we had was gained from discussions with Enron's management at that time, the new president, Greg Whalley, and CFO Jeff McMahon. They explained to us that, as much as they knew, from their investigation, there were no further partnerships that had debt obligations that they were unaware of. But that, indeed, and as my comments stated, they had not fully completed all that the investigation was to provide.

In the above example, the professional from the Standard & Poor's discusses his organization's decision not to downgrade Enron. One of the reasons offered by Standard & Poor's is that they were able to meet with the Enron's top management who explained the situation and provided updated information on the state of the investigation into the number of financial structures within the organization and on how they may impact the earnings. This kind of a quick access to information from top management is likely to make professional service firms more biased towards this particular source of information leading to the likelihood that other alternative sources may be neglected.

Another important way in which the communication between clients and professional service firms becomes easier is when key professionals from professional service firms move to the client organization. This phenomenon was particularly pronounced between Enron, Arthur Andersen and Vinson & Elkins, where senior professionals from the law or accounting firm would move to the client organization and vice versa. The extract below illustrates one such instance.

Chairman Tauzin: So you're the lead counsel for Enron. The guy Mr. Lay turns to get help with these allegations.
Mr. Derrick: Correct.
Chairman Tauzin: Formerly with Vinson & Elkins. You turn back to Vinson & Elkins to investigate it, but you tell them don't look too hard. That's the common sense review of what I've just read to you.
How do you explain that?
Mr. Derrick: I would respectfully disagree with that construction, Congressman. As I mentioned, Mr. Lay and I both proceeded in absolute good faith to take Ms. Watkins' allegations extremely seriously. What you were pointing to as the downside of Vinson & Elkins was also the great strength of Vinson & Elkins--
Chairman Tauzin: Mr. Derrick worked for many years for Vinson & Elkins on the Enron account and you were at Enron, right?
Mr. Dilg Right.
Senator Stupak: So you have 25 years there at least.
Mr. Dilg. It was 20 years, Congressman.
Senator Stupak: But Mr. Dilg, you replaced Mr. Derrick in Vinson & Elkins. It just seems like such a cozy relationship. Is it surprising that when you get a memo saying there's trouble- even the common lay person on the street can figure it out, none of you guys can figure it out?

In the above extract, Congressional Representatives try to examine why a reputable law firm such as Vinson & Elkins could not find instances of questionable accounting and dubious

financial structures singled out by some of Enron's employees. In examining the external counsel and Enron's general counsel, it comes to light that Enron's present general counsel (Mr. Derrick) was a partner in Vinson & Elkins before joining Enron, while the partner in charge of the Enron account at Vinson & Elkins (Mr. Dilg) was previously the general counsel for Enron. There were several instances where senior professionals from Arthur Andersen moved to Enron and vice versa. Such an exchange of professionals not only increases access between clients and PSFs but increases the likelihood that professionals would favor a client centric version of available information and would be more likely to reframe information to suit the client's interests.

Thus, ease of access between professionals and client organizations works in three main ways to reinforce the small world phenomenon. First, quick and easy access for some professional service firms to the top management of the client organization is likely to make them favor this particular source rather than others such as publicly available information. Second, the exchange of professionals between client organization and professional service firms increases the likelihood of cementing commitment to each others interests. Finally, a less conscious way in which ease and openness of access consolidates the small world phenomenon, is through frequency of interaction which may result in professionals paying more heed to managerial speak than professional due diligence consistent with their background.

Till now the discussion of the variables influencing the small world phenomenon have focused on aspects shared between a set of professional service firms and an influential client. It is important however to realize that the small world may not be generalizable to all professional-client relationships. In fact, some professional service firms are structured in ways that make them more susceptible to privileging client interests.

(v) PSF ethos. PSF ethos is a combination of aspects of organizational structure, an understanding of organizational goals and objectives, and the perception of the espoused model of professionalism, all of which combine to create a distinctive ambience within a PSF. One of the concerns after the Enron and Arthur Andersen failure was the potential for further such professional lapses and more corporate failures thus highlighting the

importance of examining factors within professional service firms that may influence their heightened sensitivity to client concerns. Chapter Five, 'Exploring Professional Space', discussed the discretionary use of organizational policies and a strong endorsement of the expertise model of professionalism. Therefore, it is only logical to expect that these factors will play a role in the manner by which professionals view client relationships. Professionals' attitude to work and responsibility indicate to a large extent their approach towards client relationships, as the following extract illustrates:

> **Senator Thompson:** Well, I understand that. But let me give you a cross-check on the other side of the ledger. Mr. Feygin, I was looking here at a clip from the *London Times*, March 21, 2001, where it says J.P. Morgan reins in analysts. It says that the independence of J.P. Morgan's stock research is being questioned after analysts at the U.S. investment bank were instructed to seek approval from corporate clients before publishing recommendations on those stocks. In a memorandum circulated to J.P. Morgan analysts last week, Peter Houghton, head of Equity Research, said that he must personally sign off on all changes in stock recommendations. In addition, the memo further sets out rules described as mandatory, requiring analysts to seek out comments from both the companies concerned and the relevant investment banker, J.P. Morgan, prior to publishing the research.
> He says, "If the company requests changes to the research note, the analyst has a responsibility to incorporate the changes requested or communicate clearly why the changes cannot be made."
> So it looks to me like J.P. Morgan is telling their analysts that they have got to get a sign-off from the company they are analyzing and the mortgage banking side of the operation before they can make any changes.
> **Mr. Feygin:** Thank you for the question, Senator Thompson. I have to say that I learned of this memo from the press. Peter Houghton is the head of our research franchise in London, and those rules did not apply to my actions. Until the rules were changed recently, senior analysts were not required to seek approval for ratings changes, period.
> In the initiation process for the companies that we are about to pick up coverage on, we do send part of the report to the company, what we call the back of the report, which factually describes the businesses for fact checking. But after that point, the recommendations, the evaluation, and our opinions are not second-guessed by outside or inside people.

In the above extract, the oft proclaimed assertion of investment banks, that they keep their investment and analyst functions separate, is being questioned by Congressional Representatives because of media reports that suggest that clients are very closely involved in final determination given by the ratings security analysts . Surprisingly, senior professionals from the investment bank have no other explanation to offer except that it was something that happened at the European office and is not likely to happen in the U.S.. Interestingly, what the incident really illustrates is the arbitrary and tenuous nature of practices and policies within professional service firms.

Practices such as 'Chinese walls', for the most part, are designed to keep conflicts of interest at bay. But in the case of Enron, it appears that when professionals and clients become part

of a relationship where mutual interests are constituted continually through professional decision making processes, organizational policies and practices, otherwise designed to facilitate professional due diligence, become discretionary. Adding to the discretionary nature of organizational policies and practices are incentive and reward systems within the organization that favor professional output that privileges client interests.

> **Senator Thompson:** Yes, Mr. Chairman, I was just wondering whether or not with regard to any of you or anyone on your research or brokerage sides of your companies, whether or not your compensation is in any way tied to the profitability of the investment banking side of your business, salaries, bonus, anything. Just yes or no, unless you care to elaborate.
> **Mr. Niles:** Yes, I think investment banking profitability, the profitability of the overall firm factors into my bonus, but it is a general matter.
> **Senator Thompson:** Anyone else? Is that the case?
> **Mr. Gross:** It is the same issue.
> **Senator Thompson:** Beg your pardon?
> **Mr. Gross:** It is the overall profitability of the firm where the ultimate pool is drawn from, but there is no direct link.
> **Senator Thompson:** That the bonus is dependent upon?
> Mr. GROSS. Overall profitability of the firm, yes, and the investment bank is part of our firm.
> **Senator Thompson:** Is that the same thing, Mr. Feygin?
> **Mr. Feygin:** That is correct.

In the above extract, security analysts from three of the largest investment banks are questioned about the relationship between the profitability of their investment side and their pay package. All three analysts agree that their final pay package is tied to the overall profitability of the investment side of their bank. Therefore, the small world phenomenon between large professional service firms and their clients gets reinforced not only through the interaction between professionals and clients but also through presence of expedient organizational policies that can be used to reward or punish professionals that conform to, or challenge, organizational goals and objectives.

Enormous amount of money gets exchanged between large professionals and clients, adding yet another factor that cements the small world approach. Enron, was one of the most prized clients for many professional service firms and is not surprising that many were unusually attentive to its financial well being. An idea of the extent of money involved is discerned by the following extracts:

> **Mr Berardino (Arthur Andersen):** We were paid $59 million by Enron, including $25 million for our audit. There is a perception that the remaining $27 million was for traditional management consulting work such as installation of computer systems. In fact, the bulk of that $27 million was for audit-related work, tax work and work that could only be done by auditors; $13 million was for consulting work done by Arthur Andersen.

> **Senator Greenwood:** And let me address my first question to Mr. Dilg. Mr. Dilg, you are the Vinson & Elkins engagement partner for the Enron account, and you have worked on the account since 1990, when Jim Derrick handed over the account to you when he left V&E to become Enron's General Counsel. Reportedly, Enron is V&E's single largest client. V&E billed Enron over $36 million in 2001 and over $150 million during the past 5 years. By comparison, Arthur Andersen billed $54 million to Enron in 2001. Is it true?
> **Mr. Dilg (Vinson & Elkins):** Yes.

From the above extract it would be easy to infer that professional services fees sway the extent to which professionals and clients are attentive to each others' interests. Further, this enmeshing of interests and commonality of viewpoints within a small world setting infuses certain behavioral expectations which, when breached, have negative repercussions. An instance is mentioned by the professional in the extract below:

> **Mr. Schilit:** Again, I am not part of the Wall Street establishment, but every time I have seen an analyst go out on a limb and go against the conventional wisdom, which is you have to be very positive on the companies that you are writing about, that becomes a very controversial analyst. It could be a very good career step if they want to leave the sell side and go to work for a hedge fund. In fact, there is a fellow from Lehman Brothers who wound up with a wonderful job at a hedge fund. But if you want to move up the hierarchy in the Wall Street establishment, you don't rock the boat. And that is the reason why nobody at those firms will say there is a problem at a company.

In the above extract, a professional speaks of the observed nature of the professional-client relationship. Constant interaction between a set of professional service firms and clients with variables such as ease of access, reputation, and reciprocity so entangles professional and client interests that it sets up certain expectations from professional output which, when not fulfilled, can jeopardize the career prospects of individual professionals.

PSF ethos is another important variable that influences the way in which professional-client relationships play out because it interacts with and influences other variables affecting the small world phenomenon. Large professional service firms provide a range of services to their clients thus interacting with them at many levels and through different channels which affects the ease of access between participants. Espousing the expertise model of professionalism also influences the manner in which professionals view client relations and professional responsibility. The expertise model of professionalism is more outcome oriented, focusing on tasks and endorses a rule based approach to professional work. Perception of professional responsibility based on these characteristics takes the focus away from issues of responsibility to the larger unorganized group of investors. This mitigating of

concern about the consequences of professional work for an important constituent external to the professional-client relationship further reinforces the small world phenomenon.

Summary

The notion of the small world of professionals and clients makes the concept of client capture quite complicated. Client capture, as discussed earlier, suggests that large influential clients by virtue of their size, expertise and bargaining power can influence PSFs to cater to their interests. A preliminary look at the failure of Enron and the defense of the PSFs would suggest that the thesis of client capture holds true for this situation. However, a closer look at the relationships shared by Enron and the PSFs and the notion of the small world underlines the importance of examining the dynamics of relationships between large firms and clients, and therefore the concept of client capture in more detail. The small world phenomenon suggests that client capture is much more than the exercise of asymmetry of power in dyadic relations; it is a result of the extensive interaction between professionals and a client which also reflects the influence of the organizational forms in which professionals work and their perception of professional responsibility. Client capture is a gradual and cumulative process of making choices, of being cognizant of mutual interests, and of being attentive to intangible cues such as reputation, status, and reciprocity which inculcate commitment and reinforce the relationship.

Discussion and Conclusion

The concept of the small world highlights several interesting insights. First, relationships between large clients and professional service firms are rarely dyadic. Most large firms have several PSFs working simultaneously on different projects. Not only do client firms have a preferred set of professional service firms to interact with; in providing their clients with different kinds of services, PSFs are in continuous contact through multiple channels. Second, professional decision making is influenced as much by the interaction between clients as it is by the interaction between the different professional service firms. PSFs constantly allude to the reputations of other involved PSFs to explain their participation or

their choice to endorse client sponsored structures. Third, the incentives to maintain relationships are not only because of commercial considerations or reward systems within PSFs. Large PSFs target similarly large clients who often share directors across different boards. Endangering the relationship with a client may also put their other client relationships at risk. Fourth, professionals and clients are enmeshed together because they define, negotiate, and collaborate on issues of mutual interest. As is evident from the results, it is very difficult to point out when Enron is more powerful or when the professional service firms dictate terms. The decision making process and subsequently professional work is fraught with designing and executing equity structures that simultaneously cater to both the client's and PSF's interests. Fifth, small worlds get cemented not only through consistent interaction but also by the unique ethos of some professional service firms. When PSFs endorse the expertise based model of professionalism which focuses more on the outcomes generated, have practices and policies that are utilized based on the kind of client and the nature of the relationship, and have incentive systems that reward client oriented outcomes professionals in such organizations become more cognizant of and committed to client centric results. Finally, the small world concept suggests that embeddedness of clients and professionals takes place gradually, over a period of time because of repeated ties and constant catering to mutual interests, which creates a situation where professionals are impervious to alternate sources of information and insulated from any issues of public responsibility except their own interests.

Enron and the failure of Arthur Andersen highlighted the importance of revisiting the literature of professional-client relationships. Extant literature on professional-client relationship tends to treat the relationship in a dyadic manner (a client firm interacting with a PSF), focusing on a single event, finding the dominant partner in the dyad, and explaining the outcome based on the asymmetry of power. Even though this scenario may hold for certain kinds of professional-client relationships, Enron and its associated PSFs presented a very different example. Enron was a very large reputable client involved in many endeavors requiring professional services from different PSFs at the same time. The PSFs that interacted with Enron were themselves quite large and equally reputable and did not *solely* depend on this client for their commercial well being. Given the apparent equity between professionals and clients in terms of power and status, one would have expected that these

PSFs would not hesitate to protest against Enron's questionable deals, accounting choices, and financial structures. Instead what came to the fore was a scenario where most PSFs involved – auditors, external counsel, investment banks, security analyst firms, and credit rating agencies willingly and uncritically abetted and endorsed Enron's choices.

Client capture and the concept of the small world of professionals and clients give an insight into the numerous influences that operate on relationships between large clients and large PSFs. The concept of the small world is not entirely new. It is one form of social organization that has received a great deal of attention for its possible ability to influence creativity and performance (Uzzi and Spiro, 2005). Although not universal, small worlds have been found to organize a remarkable diversity of systems including friendships, scientific collaborations, corporate alliances, interlocks, the Web, power grids, a worm's brain, the Hollywood actor labor Market, commercial airline hubs, and production teams in business firms (Watts, 1999; Amaral et al 2000; Kogut and Walker 2001; Newman 2000, 2001; Davis, Yoo and Baker, 2003; Baum, Shipilov and Rowley 2003; Burt 2004). Uzzi and Spiro (2005) argue that a small world network governs behaviour by shaping the level of connectivity and cohesion among actors embedded in the system (Granovetter 1973; Freidkin, 1984; Newman 2001; Moody and White, 2003; Watts 1999).

Although the term 'small world' is borrowed from the literature on social networks, its use in the context of professional-client relationship along with the inductive approach of the empirical study contributes to a better appreciation of the notion of small worlds. Traditionally the research on small worlds has highlighted the benefits that accrue to participants, which include lower transactional costs, access to rich and fine grained information which otherwise would not be available, to talent in the case of the Broadway musicals, and to influential board member and director connections that not only increase the prestige of the boards but also give it access to other reputation rich boards (Kogut & Walker 2001, Davis, et al., 2003; Uzzi & Lancaster, 2005).

However, in a very recent call for papers for a special issue in Organizational Science, the editors suggest much of the literature on networks "presents a rather unbalanced picture. Specifically, while an extensive body of knowledge exists on how network structures may

contribute to the creation of outcomes at different levels of analysis (individuals, groups, organizations and population of organizations), less attention has been paid to understanding how and why networks emerge, evolve and change" (Ahuja, Soda, Zaheer 2007; Call for papers). Keeping in mind the above statement, the small world of professionals and clients contributes to network theory in two key ways: first; the small world of professionals and clients is a specific kind of a network of interorganizational ties. Much of the research on network theory examines interorganizational relationship through tie formation *without* examining the different *types* of ties that can exist between organizations. By focusing on specific categories of interorganizational ties, we can gain a richer and more nuanced understanding of how different types of network may evolve, engage, and sustain themselves. For example, professional-client ties are likely to have very different dynamics of emergence and evolution compared to ties between organizations involved in strategic alliances. Further, networks of a certain type such as those between professionals and clients are likely to have serious implications for investors, which can only be examined if the categorical differences between ties were acknowledged to play a central role in network dynamics. Second, the small world of professionals and clients by focusing on the factors that influence the interaction between the different participants in the network (such as ease of access, reputation, mutual interest, and reciprocity) contributes further to understanding the dynamics that lead to the emergence and perpetuation of such networks.

The small world of professionals and clients though similar to small worlds everywhere, is unique because of the involvement of professionals. Professionals in our society play extremely important roles. They are seen as creators, carriers, and clinicians within the social environment (Scott, 2007). As creators, professionals augment and evaluate knowledge systems; as carriers, they transport and translate knowledge into practice and therefore are responsible for substantial innovation. As clinicians, they apply knowledge to individual cases. In the case of the small of professionals and client, such as that of Enron and its associated PSFs, because of the reputation and status of the organizations involved, professionals end up playing a little of all three roles. Previous research on the innovative abilities of professionals has highlighted the role of elite PSFs in facilitating change within the professional field whether it is through theorization (Greenwood, Suddaby, Hinings, 2002; Greenwood et al 2006), through alternate hiring practices (Sherer and Lee, 2002) or

through generating new practice (Anand, Gardner and Morris, 2007); elite PSFs possess the knowledge to innovate, credibility to translate, and the expertise to generate new practice areas. Even in the case of the PSFs that associated with Enron, the accounting firm was one of the pioneers of the mark-to-market form of accounting which Enron and lot of other large firms used; Arthur Andersen was also in the forefront in devising innovative equity structures, just as Citigroup professionals specialized in novel financing arrangements.

However, within a small world setting the knowledge, innovation and practice gets grounded in instrumental intent and divorced from societal obligations that are expected of professionals. One of the most surprising and, to some extent, disturbing things to emerge from the Congressional Hearings was the utter lack of societal responsibility in professionals from large PSFs. Most of them argued that they were professionals because they followed rules and regulations, they fulfilled their limited tasks in their niche specialties but there was hardly any mention of the responsibility to the public. Given the important roles that professionals play, in general, and the unique resources that elite PSFs possess in terms of influencing professional practice – the presence of small worlds threatens to alienate further the idea of societal obligations from professional behaviour. Enron and the spate of subsequent corporate scandals found many other similar PSFs liable. Changes were made to regulate the accounting profession and other professional associations such as the Association for Security Analysts voluntarily revised their code of ethics. It would be interesting to examine whether enforced and self enforced changes have resulted in any shift in the notion of what constitutes professional behaviour.

Chapter 8
Conclusions

Introduction

This thesis was motivated by an attempt to understand factors that influence professional behaviour. One of the key triggers for this question was the sudden failure of Enron, which was then followed by a spate of corporate scandals. Surprisingly, many of these scandals revealed that some of the most prestigious professional service firms in the world worked in close complicity with their clients to present a picture of financial well being to the investors which in most cases was questionable and in some cases even fraudulent. Events such as the collapse of Enron and the subsequent failure of Arthur Andersen raised two central questions regarding professional work and responsibility. (1) How do organizational forms where professionals work influence professional behaviour? (2) What is the influence of client relations on professional behaviour? The literature on professionals and organizations, and professional-client relationships offered helpful but inadequate insight into the manner in which large professional service firms influence perceptions of professional responsibility and also towards examining the influence of client relationships on professional behaviour. Therefore, the central motivation of the thesis was to examine the concept of professional behaviour and the influence of two key factors on it: organizational forms where professionals work; and, client relations.

This Chapter highlights the main findings of the thesis and links them to broader ideas of change experienced by professions and the shift in the dynamics between professions and society. The Chapter is divided into four parts: the first part revisits the original research question and summarises the findings; the second part highlights in the concepts generated from the empirical studies, their contribution and their research potential; the subsequent section ties the concepts together; and the final part discusses the limitations of this thesis.

Professional Behaviour, Professionals and Organizations and Client Relationships

The main object of the thesis was to examine the notion of professional behaviour by focusing on two key variables that influence professional work: organizational forms where professionals work, and client relationships. Empirically the questions were examined using the transcripts of the Congressional Hearings related to the collapse of Enron and the failure of Arthur Andersen. The Congressional Hearings contained rich data consisting of accounts from professionals from different organizations – Enron, Arthur Andersen, Vinson & Elkins, premier investment banks, credit rating agencies, and security analyst firms – all geared towards providing their perception of what *really* led to the failure of one of the largest and most successful corporations in the world, and the downfall of one of the Big Five accounting firms. This database of professionals' accounts addressed aspects of work, decision-making, client relationships, and perception of professional responsibility, and therefore was an appropriate avenue to examine the research questions.

Chapter Two discussed the research on professionals and organizations and professional-client relationships. The literature on professionals and organizations was important in understanding the various streams that have examined the interaction between professionals and the organizations in which they work. This body of work indicates that there are at least three different ways in which professionals' experience in organizations can be explored. First, through the lens of the organizational professional conflict (OPC) thesis which suggests that professionals who work in bureaucratic organizations experience role conflict, stress, lower professional commitment, and decreased job satisfaction compared to professionals who work in 'professional organizations' (i.e., organizations such as professional service firms, that are owned and managed by professionals). The second stream of research examines more the long term consequences for professionals working in bureaucracies. This stream, termed as the Proletarianization thesis, proposes that professionals who work in bureaucratic organizations, over time become more committed to their organization than to their profession, that is, they lose their professional identity. The final stream of research, the Adaptation thesis, suggests that most organizations, even bureaucracies, are sensitive to the values cherished by their professional workforce and hence try to accommodate them by structuring their in-house professional departments to

resemble professional organizations. In sum, the research on professionals and organizations offers three key insights:

- Professionals possess a set of 'professional values' such as autonomy, discretion, peer review, and collegiality that appear to be absolute constructs which are central to the professional identity. The loss of these values signals, to a large extent, loss of professional identity.
- Some organizational forms such as bureaucracies because of their formalised structure and centralized authority are incompatible with professional values and therefore are 'unfriendly' to professionals.
- The corollary being, organizations such as professional service firms, where ownership and management is dominated by professionals, are much more likely to nurture professional values and are therefore more professional friendly.

Even as these streams of literature are helpful in understanding the professionals' experience in different organizational forms, they were inadequate in explaining what happened in the case of Enron. Here, professionals in an organizational form allegedly 'unfriendly' to professionals exhibited behaviours that were termed 'professional' by Congressional Representatives. These set of behaviours included voicing dissent over inappropriate professional choice, questioning the intent and consequence of professional work and privileging the interests of the investor. These behaviours were absent in all of the large professional service firms that associated with Enron. But professionals in these PSFs argued that their professionalism could not be doubted either. The different versions of professionalism resembled Brint's (1996) models of professionalism – the social trustee and the expertise based model indicating that there may be *multiple* ways of perceiving professional responsibility. The above observations led to the first subsidiary question: *what are the factors that enable or constrain the presence of particular models of professionalism in certain organizational forms?*

The other key variable to influence professional behaviour was client relationships. The concept of client capture offered a meaningful way to connect the influence of client relationships on professional behaviour. Client capture addresses a specific set of professional-client relationship, one that is shared between large professional service firms

and their clients. The concept of client capture suggests that large clients possess sufficient expertise to influence the work and decision-making of professionals. A review of the research on professional-client relationships indicated that there were two main streams in this body of work. The first one was termed the 'characteristics approach' and examined the individual professional-client dyads, and characteristics of organizations where professionals work, as well as client attitudes. The main focus of this stream of research was to examine whether compatibility in professional-client characteristics could lead to better client satisfaction. Another focus of this stream of research was to understand the effect on client satisfaction when professionals start working in bureaucracies, and the influence that formal structures have on access, service delivery, and the satisfaction of clients. The other major stream in the professional-client relationship literature focused on the power inequity approach which suggests that professional-client dyads, whether they are individuals or organizations, are engaged in attempting to attain their own ends. The general approach in this stream of research focuses on a single event, and explains the outcome on the basis of the relative power inequity. In summary, the research on professional-client relationships offers the following insights:

- Professional-client relationships are examined as primarily dyadic relationships where either complementarities of characteristics or power inequity ensures client satisfaction.
- As the majority of the studies focused on single events, there is a general lack of attention given to the actual dynamics that sustain professional-client relationships.

Although this body of research was helpful in understanding specific kinds of professional-client relationships, Enron and the PSFs associated with it presented a different problem. A preliminary read through the data indicated that Enron had several projects going on simultaneously involving several professional service firms. In such a case, the dyadic approach would be quite difficult to follow. In addition, the power inequity approach also appeared inadequate because Enron associated with very large and very prestigious professional service firms who had many similar clients. Therefore, there was a need to find a concept that specifically addressed relationships between large corporations and large PSFs. The concept of client capture offered the opportunity to examine the relationship between Enron and its PSFs and the consequences for professional behaviour, thus setting

up the second subsidiary question: *How do large PSFs get captured by their client and with what consequence?*

Main Contributions and avenues for further research

The main contributions of the thesis are in three areas: probelmatizing the idea of professional behaviour; draw attention to concepts such as client capture that allow for richer understanding of a particular set of professional-client relationships; and, focusing on avenues such as Congressional Hearings as sites to examine contestations between competing models and policy making.

Professional Behaviour. With the rare exception of Brint (1996) who suggested that the notion of professionalism changes with time, it is only recently that researchers are highlighting the importance of examining professional behaviour, not as an absolute construct, but more as behaviours engaged by professionals that are influenced by the context within which they operate (Cooper & Vaughan, 2005; Suddaby, Gendron & Lam, 2007).

The idea of 'professional behaviour' has traditionally been imbued with more normative value than being viewed simply as behaviours that professionals engage in. In Chapter 2 I discussed how professional behaviour came to be so value ridden. To recapitulate, earlier studies of professions emphasised the importance of professionals engaging with the acquisition of the specialized knowledge that constituted their profession. It was through the expertise gained through this engagement, and a complete absorption in the work that would eventually enable professionals enough experience to contribute meaningfully to society (Meadows, 1946; Greenwood, 1957). Gradually, the expectation of service orientation or a commitment to public good became one of the essential traits of any profession – a kind of payback to the public for the privilege of self regulation (Moore 1970). Behaviours constituting 'professionalism' included 'honourable conduct, self control and the discipline of wayward brethren' (Moore, 1970). Surprisingly, in over thirty years there has been little change in our expectation of what constitutes professionalism or professional behaviour. In fact, the expectation of service orientation or the idea of the professional as the public

watchdog now dominates all other aspects of professional work (Moore, Tetlock, Tanlu & Bazermann, 2006).

One of the reasons of the survival of the trait based approach to professionalism is because the dominant view of professionals continues to be that of a community invested with social trust which needs little outside supervision; however, the scandals associated with the professions suggest that internal controls within professions are fairly inadequate. Research on deviance in professionals up until the 1990s suggests that professionals are more likely to engage in deviant activities in organizational forms where their role sets require 'contradictory postures', i.e. deference to sets of expectations that are vastly divergent such as keeping up with the norms of societal obligations *and* valuing organizational goals and activities (Kempler 1966; Payne 1980; Raelin 1994). Such studies reinforce the unchanging inertial view of professionalism, and in doing so underplay the role of the employing organization *and* professionals in negotiating organizational and professional pressures.

This thesis, by focusing on two different models of professionalism – the social trustee model, and the expertise based model – and by exploring the manner in which different organizational forms enable or constrain their expression, problematizes the idea of professional behaviour. The motivation in the two empirical studies has been to emphasize the importance of situating professionals' behaviour in more grounded context, that is, in the organizations that they work and the client with whom they interact. In examining the behaviours of professionals more as an amalgamation of influences generated from the employing organization's goals and values, the pressures faced by specific types of organizations (such as large professional service firms) and the influence of client relationships, the studies raise questions about issues such as professional ethics, the source of and the importance of socialization of professionals and their engagement, if any, with societal obligations.

This approach to behaviour is advantageous for three reasons. First, it enables us to move away from the idea that professionalism is an attitudinal construct somehow directly related to individual traits and disposition, therefore to some extent questioning the 'rotten apple' thesis that is frequently offered as an explanation for professional misbehaviour (Gunz &

Gunz, 2006). Methodologically, too, it entails a shift away from pre-fabricated surveys that tap into the 'professional traits' approach, highlighting the need to design and conduct research studies sensitive to the relationship between context and behaviour. The final advantage of this approach is that it provides a way to link two parallel but mostly unrelated streams of studies within the sociology of professions literature. For example, a vibrant research stream examines changes in organizational form and governance structures in professional service firms and relates them to market or institutional pressures (Greenwood, Hinings & Brown, 1990; Hinings, Brown & Greenwood, 1991; Cooper, Hinings & Greenwood, 1996; Pinnington & Morris, 2003; Greenwood & Empson, 2003; Empson & Chapman, 2006; Malhotra, Morris & Hinings, 2006). Yet another stream focuses on professionals' attitudes and professional ethics, examining issues more at an individual level (Bartol, 1979; Welsch & LaVan, 1981; Frankel, 1989; Blau, 1999; Anderson-Gough, Grey & Robson, 1998; 2000; Gunz & Gunz, 2006). However, there is inadequate attention paid to research that connects these two streams. A case such as Enron, its relationship with large and reputable professional service firms, and the difference in perceptions of professional behaviour observed in different groups of professionals offers the opportunity to create linkages between the macro level changes experienced by professional service firms and their influence on the manner in which professionals behave.

Professional Space. Related to the idea of professional behaviour and building on the importance of creating linkages between context and behaviour is the notion of *professional space* that was introduced in Chapter 4. Professional space taps into the notion that behaviours that are deemed professional, such as voicing dissent against professional choices that appear inappropriate, privileging the interests of the large group of unorganized investors, and internal whistle blowing, are not entirely the result of individual volition. To a large extent these behaviours are enabled by availability of multiple repertoires of acceptable actions, that is, different models of professionalism. One of the key puzzles that motivated this thesis was the effort to understand why professionals in a corporate bureaucracy, Enron, an organizational form traditionally seen as inimical to professional commitment, were able to exhibit what was viewed as 'professional behaviour'. In contrast, none of the professionals in organizational forms viewed as 'professional friendly', such as professional service firms, provided any example of similar behaviours.

The results suggest that organizational forms able to accommodate multiple models of professionalism provide professionals with a wider repertoire of acceptable actions. Specific aspects of the organizational form, such as the clear divisionalized structures which contained the more formal corporate bureaucracy along with the in house professional departments, presence of regularly *utilized* formal policies and processes, and clear incentive systems that harmonize with organizational goals and objectives, enable professionals in this organizational form to accommodate both the traditional social trustee model of professionalism and the expertise based model of professionalism.

In addition to the clarity and complexity of organizational structures and systems, there are other factors that indicate why corporate bureaucratic forms are more amenable to accommodating multiple models of professionalism. In an organizational set up where professionals are not solely responsible for organizational continuance and revenue generation, where their main agent and continued source of socialization is likely to be the professional association, where professionals are outnumbered substantially by non professional colleagues, and where they can be transferred across divisions easily – the social trustee model offers a useful strategic repertoire of values that enable professionals to differentiate themselves from non professionals. The core characteristics of the social trustee model in privileging professional autonomy, discretion and societal obligations, package attractively a set of values that are broad enough to be transferred across organizations and divisions, yet specific enough for professionals to continue to maintain some sense of control over the content and process of their work.

Compared to the corporate bureaucratic form, the professional service firms present a very different picture. The results indicate that most large professional service firms have comparable extents of formal structures and systems in place. What distinguishes these large PSFs from the corporate bureaucracy is the *perception* of the importance of these structures. Professionals in PSFs tend to use policies, processes and systems *strategically* in order to attain well understood goals and objectives. Part of the reason for this strategic use is the fact that professionals in large PSFs are solely responsible for revenue generation and the continuance of their organization. They are also more likely to have experienced stronger socialization by

their employing organization, making them more attuned to fulfilling organization specific goals and objectives. Large PSFs in turn experience the tension to balance commercial aspirations with expectations of societal obligations (Greenwood, Suddaby & McDougald, 2006). These contradictory tensions are resolved to some extent by espousing the expertise based model of professionalism which is more outcome-oriented, privileges the market as the ultimate arbitrator of professional expertise, and effectively marginalizes the role of any constituent outside of the professional-client relationship.

The concept of professional space is interesting for two reasons:

- It is a concept that connects the environment within which organizations operate with the influence that some salient aspects of it may have on the way professional work and responsibility is envisaged.
- Professional space privileges professionals' interpretive scheme, that is, it emphasises the importance of focusing not only on shifts in formal structures and arrangements as a definite statement of change but also on examining the shifts (if any) in the manner in which professionals *interpret and interact* with these changes. In doing so, professional space, while remaining grounded in the organizational forms, connects broadly with the macro conversation about archetypes and logics (Greenwood & Hinings, 1996; Greenwood, Suddaby & Hinings 2002; Thornton & Ocasio, 1998).

Avenues for future research: Recent studies have highlighted the importance of examining shifts in the forms of governance and the variation around the 'traditional structural archetype, the P2 form' (Empson & Chapman, 2006; Malhotra, Morris & Hinings, 2006). The authors suggest "Firms are moving away from these archetype under pressure from market and institutional influences, toward diverse forms: of these forms, some mimic corporate structures…; other versions are more loosely coordinated." (Mahotra, Morris & Hinings, 2006: 196). A natural and logical extension of this line of research would be to understand the manner in which each of these different organizing arrangements influence and interact with the different models of professionalism, thus influencing professionals' abilities to maneuver organizational and professional concerns (i.e., professional space). Not only will the variation in organizational arrangements influence professional space, but it is also likely to be influenced by different professions. For example, one could assume that in

professional service firms that are more likely to have a networked structure with groups of professionals from different professions being brought together to work in teams, there is a higher probability of the existence of a constant tightrope-walking between values endorsed by different professions, the organization, and the broader norms. Therefore, with the focus of research in the sociology of professions being directed towards understanding variance in organizational forms, the concept of professional space too appears to be a potent area of future research.

Given that Professional Space as a concept taps into the ability of professionals to negotiate organizational objectives and professional expectations; it has several other avenues for further research especially in empirical settings where professions are granted more 'autonomy'. A significant development such as this would necessitate a renegotiation of influence or control between the employing organization and the professionals who work there. New developments in the fields of pharmacy and nursing highlight the potential of professional space as a way of understanding the interaction between organizational forms and professionals. In the first case, pharmacists in Canada were given the authority to prescribe and modify certain categories of medication for patients; in the second, nurses in the United Kingdom were given the authority to perform resuscitation on emergency patients *without the presence of a physician.* Both these changes set up two challenging and interesting dynamics that can be examined using professional space.

The first involves reframing of notions of what 'professionalism' is, i.e. the professional community of pharmacists and nurses taking into account the broadening of their jurisdiction may endeavour to reframe and reposition their conception of professionalism to gain more autonomy over their work. In doing so, they inadvertently set up another dynamic – the renegotiation of 'professional space' between professionals and their employing organizations. To illustrate, a large proportion of pharmacists are employed in large corporations such as WalMart, where pharmacy is but one aspect of the gamut of goods and services provided. In this scenario, pharmacists in these organizations are at best a small part of the larger group of non professional employees. With jurisdictional broadening, it is likely that this group of professionals may attempt to acquire more control over their work-content and process. That is where the usefulness of a concept such as professional space

plays in. It is dynamic enough to acknowledge and accommodate changes that occur in the work environment of professionals and the manner in which professionals are likely to deal with it.

In the case of the nurses in the United Kingdom (who can now perform emergency resuscitation procedures on patients *without* the presence of a physician or consultant, similar renegotiations are likely to be set up not only with the employing organization, but also an additional set of influence- the physicians whose turfs they are encroaching. Therefore, taking into account the recent changes, professional space for nurses in the United Kingdom not only is a function of the organizational form that they are part of, but also includes their changing dynamics with other professions that overlap certain areas of their functioning.

Professional behaviour and professional-client relationships. Just as professional space attempts to link professionals' behaviours to the organizational form that they work in, the *small world of professionals and client* attempts to relate professional behaviour with another important variable – client relations. One of the more disturbing outcomes of the collapse of Enron and the failure of Arthur Andersen was the fact that very large and reputable professional service firms were actively colluding with their client to generate professional output that made Enron appear as an attractive proposition for institutional and individual investors. Extant research has highlighted the importance of reputation for professional service firms because of its role as a social cue for quality and status (Uzzi & Lancaster, 2004; Greenwood, et al., 2005). Therefore, these corporate scandals were even more surprising because professional service firms were risking their core asset in being complicit with their client's activities.

In order to understand why large professional service firms would acquiesce to such (mis)behaviour, I used the concept of client capture. Client capture examines a specific set of professional-client relationships, that between large professional service firms and their clients. It suggests that because of the available expertise with large clients, they may influence professionals to cater to their specific interests. Although at a preliminary glance Enron and other corporate scandals bear out this inequity argument, the results indicate a more complicated story.

The relationship between large professional service firms and Enron, contrary to much of the literature on professional-client relationships, was rarely dyadic. Enron (similar to large corporations of that size) would have multiple projects that went on simultaneously involving many different, equally large PSFs. In such a work arrangement, the client becomes an influential connecting node for several professional service firms. Working in such close proximity over time inculcates a sense of comfort that is reinforced by the easy access between the members of the small world, the shared reputational capital, the sense of reciprocity and access to informal information. All of these factors create a social bubble around the participants of the small world, which filters information. Eventually it creates a shared framework of interpretation which privileges each others' interests over all other concerns. In sum, the concept of the small world of professionals and clients explores the enmeshed relationships between a group of professional service firms and an influential client.

One of the interesting insights from the study is the potential of small worlds to turn into a framework that becomes an interpretive mechanism for all the participants in it. It has the potential of turning available data to which choices deemed as appropriate (by the participants) are yoked, thus leading to decisions that seem apt to the participants but would surprise an outsider. Therefore, within the sociology of professions an understanding of the small world and the factors that contribute to its sustenance is important because of the consequences it eventually has on an external constituent – the investing public. In the case of the professional service firms involved with Enron, the gradual enmeshment of their interests with those of their clients led to the complete disregard of the larger picture where institutional and individual investors depended on their judgement and objectivity to make investing decisions.

In summary, the concept of the small world of professionals and client is interesting for several reasons:

- It highlights the importance of moving away from the dyadic approach of examining professional-client relationships and the importance of situating such studies in their

own unique context. The small world also emphasises the role of organization size, status, and interests in influencing unique types of client relationships.

- The small world of professionals and client allows for a more nuanced understanding of the professional-client relationship because decision making here can be understood as a gradual process of cementing relations by catering to mutual interests.
- It helps in relating the idea of professional behaviour not only with *where* professionals work but also with *whom* they interact.

Avenues for further research. The concept of the small world opens several avenues for further research within the sociology of professions. As a concept that connects notions of professional behaviour with aspects of organizational forms and client relations, it provides the opportunity to examine how major changes in governance arrangements (such as shifting from a limited liability company to publicly quoted one) influences the dynamics between professionals, clients and perceptions of professional responsibility to investors *and* shareholders.

Another possibility related to the small worlds is to explore the manner in which professional-client relationships could be structured *without* ignoring the interests of the investing public. In order to understand how best to manage large client large PSF relationships, additional factors such as the role of the environment within which these relationships operate and the influence of regulators/regulations becomes important. In a recent paper, Coffee (2007) suggests that the failure of professionals to function as 'gatekeepers' was partly a function of an optimistic economy which pushed large firms to accomplish unrealistic goals every quarter. This pressure translated into clients impelling PSFs to device financial structures and instruments that were innovative (in Enron's case, questionable and even fraudulent). Thus the economic environment acts yet another factor in understanding the emergence and evolution of the small world of professionals and clients. Post Enron, new policy changes have attempted to regulate professional-client relationships. For example, organizations are now required to rotate their external auditors after every three years. Also the top management by signing on the financial statement shares liability in case of financial fraud. Such changes indicate two possibilities: first,

professional-client relationships may shift towards being more transactional, rather than social and accommodating; second, PSFs and their clients value the social aspects of their relationships enough to devise stratagems to manage these new regulations. Each of these scenarios will lead to different dynamics in professional-client relationships thus emphasizing the importance of further research in this area.

Another area which could be explored using the concept of the small world is examining situations where small worlds are useful or beneficial. Arguably, many large client organizations are in similar relationships with large professional service firms. But corporate failures similar to Enron are not an everyday occurrence which suggests that we need ot understand the manner in which 'normal', non-dysfunctional professional-client relationships are structured. Do these non dysfunctional professional-client relationships exhibit characteristics similar to the small world? If not, which variant of professional-client relationships enables the accommodation of most participants' interests, including that of the investing public; if all professional-client relationships exhibit traits of the small world, in what ways are dysfunctional small worlds different from 'normal' small worlds? In sum, the concept of the small world of professionals and clients enables the examination of a specific set of interorganizational relationships keeping in mind the contextual environment within which these firms operate.

Congressional Hearings. The final contribution of the thesis is in highlighting the research potential inherent in structured settings such as Congressional Hearings. A major focus of the Congressional Hearings related to Enron, was to understand the factors that led to the failure of such a large organization. However, substantial attention was focused on discussing the steps necessary to prevent similar failures; which makes structured sites such as Congressional Hearings very interesting. They become potent avenues for observing the links between organizational actions and policy outcomes. Recent studies in business research have highlighted the need to focus on examining consequences of organizational research on both practice and policy. Focusing on cases such as Enron offers the opportunity to examine the interplay or power and interests between key institutional representatives (i.e. representatives of the State, of the professions, and of organizations) that

lead to agenda setting, development of policy proposals and the struggle for adoption of particular proposals.

As Congressional Hearings are not avenues where judicial decisions are made, they become sites where alternate models/ logics along with their champions actively lobby for support. In that sense the Hearings form a rich research site to examine the strategies – especially rhetorical - employed by competing groups. In the case of Enron, by enabling senior professionals from elite professional service firms, representatives of professional associations and Congressional Representatives to gather at the same setting, the hearings provide a rare conglomeration of most major actors that not only influence the field of professions but also actively vie to impose their version of a preferred model.

Tying it all together

One of the most challenging tasks of ending a thesis project is to step back, take account of the results, and ask the much dreaded question, 'so what?'. This last section discusses the manner in which the concepts generated from the two empirical studies – professional space, and the small world of professionals and clients - help to illuminate aspects of professional work and behaviour. Given that the thesis project started with my interest in understanding the failure of Enron, and especially the role of the professions in it. A natural and perhaps logical contribution of the thesis would be in the area of organizational deviance.

Much of the research in deviance is divided into well bounded streams: criminology; individual deviance, which includes trait based studies dealing with violence in groups, families and other structured settings; and others that focus on unlawful acts committed by individuals (including professionals) within an organizational context. Even though the research is bounded by specialized niches, they all share some salient characteristics. First, deviance is viewed as an 'extraordinary' act, i.e. completely unanticipated and contrary to norms, goals, and objectives. Viewing deviance as an act out of the ordinary repertoire of actions necessitates tracing its source to conscious agentic activity –in short, to individuals. This focus on individual traits, dispositions, and actions forms the second salient

characteristic. Finally, in studies that focus on specialized occupational groups such as the professions; deviant actions are traced to role conflicts. That is, in consonance with the OPC thesis, these studies suggest that when professionals have to manage a wider variety of goals and objectives that may be contradictory in nature, they are more likely to take deviant actions. Although much of the research on deviance continues to focus on individuals, a small but influential body of work examines organizational deviance. This stream of research relates individual deviance to organizational processes, systems, and structure. Even as the studies move beyond the focus on the individual to more organization specific variables, they continue to be characterized by one key feature – deviance is seen as, "an activity occurring in a formal organization that deviates from both formal design goals and normative standards or expectations, either in the fact of it's occurrence or in it's consequences; and produces a suboptimal outcome…" (Vaughan; 2002: 273).

Comparing the insights of this research with the examination of the failures in the professional service firms result in two interesting observations: first; the actions defined as deviant in the literature are almost synonymous to 'unlawful' action. This contrasts with what happened at the Congressional Hearings. PSFs involved with Enron *did not* indulge in 'unlawful' activities. In fact all the senior professionals representing the large PSFs cogently argued that the firms adhered to the rules regulating their professions. One could argue that despite the rule following there was a breach of normative expectations in terms of the lack of accountability to the investing public. However, a counter to that line of reasoning would be that different groups of professionals viewed their responsibilities (including that to the public) in different ways. Therefore, the debate in the Congressional Hearings was not as much about deviant action but more about alternate and multiple conceptions of professional work. In that sense, deviance is not an extraordinary act but one of the many alternate views of acting/work.

The view of deviance as part of a repertoire of actions is not entirely novel; Bensen and Gerver, in 1963 suggested that deviance appeared extraordinary only because we tend to view organizations as 'systems that have well defined ends'. In their words,

> "If one takes the opposite view that systems do not have ends, only people do and that the collective behaviour of persons in a stable group or organization represents an

accommodation of differing (but socially developed) ends and interests, in which cooperation is an implicit transaction, containing elements of coercion, sanctions, genuine cooperation and altruism then the entire problem becomes a different one. Deviance then is simply the acceptance or non acceptance of these rules in terms of implicit or explicit estimates of consequences of conforming to or rejecting the norms of others, especially the norms of those who have authority. Deviant actions thus are not a separate category of actions, defiant of the central ends of a total system, but are simply part of the totality of actions that make up hundreds of transactions in an organization." (Bensen and Gerver; 1963: 117)

In addition, Coffee (2006) suggests that professional work during the time of an irrationally optimistic economy is more a result of the lack of deterrence mechanisms within the institutional environment and the pressure to conform to unrealistic expectations rather than pure deviousness of individuals. The above views combined together suggest that the interaction of macro environment influences (such as the state of the economy) along with interorganizational ties (such as client relationships), coupled with the unique 'ethos' within some PSFs creates an environment which makes some models of professionalism (i.e. the expertise based model) more attractive. In order to understand and examine, first, the existence of these alternate models, and then the conditions under which they are likely to appear legitimate, we need concepts that are 'value neutral'. This is where the contribution of 'professional space' and the 'small world of professional-client relationships' becomes important.

Both concepts allow for the interplay of multiple models in understanding how professionals may negotiate organizational and professional tensions. They also provide the link that relates their behaviour not only to *what* professionals do, but also to *who* they work with. By being value neutral both the concepts, professional space and small worlds, can be used to explore not only what is termed as deviant behaviour but also 'good' behaviour. Therefore, both these concepts possess the potential to address the call for studies that move away from large scale generalization to richer, more nuanced, and context specific studies of the professions and their changing environment.

Limitations

Even as the collapse of Enron, its relationships with elite professional service firms and the collapse of Arthur Andersen provided a case rich enough to explore the manner in which conceptions of professional behaviour get influenced by aspects of organizational forms and client relations, the study suffers from two key limitations: first, the nature of the data; and second, the problem of generalizability. The Congressional Hearings related to Enron provided the majority of the data that was analysed in this study. Publicly available transcript datasets, in spite of being extensive and detailed, are always to some extent inadequate because they are not collected by the researcher themselves. For example, in my study the central research questions focused on exploring the influence of organizational forms where professionals work and client relationships on professionals' behaviour. For the most part my study was helped by the fact that although Congressional Hearings were not geared towards 'judging', key participants, such as some of the top management from Enron, senior accountants, lawyers, bankers and analysts, most of whom were senior partners at prestigious professional service firms, were keen to offer their version of what led to the collapse of Enron. However, for the very same reasons, Congressional Hearings also became an arena where the discussion, on many occasions, became disconnected from what happened at Enron, but addressed a broader discussion about the relationship between different professions and the state.

Later, as the Hearings became an object of media attention, there was a gradual ebb in the number of key players directly involved in the Enron case and an increase in the number of professionals, academics, and other policy experts keen to put forward alternative views of professional work, regulation and societal obligations. They found the Congressional Hearings an influential and appropriate arena for such a discussion. Even though these discussions were interesting, they took attention and time away from *actual* events and accounts of what happened at Enron. In order to take care of this limitation the data had to be substantiated through other secondary material.

However, on balance the Enron transcripts provide an intriguing and informative window into professional behaviour, and this thesis has attempted to draw theoretical insights from them.

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